S&P Global
Ratings

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Global Banks 2019 Outlook: Bracing For More Volatility

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Contents

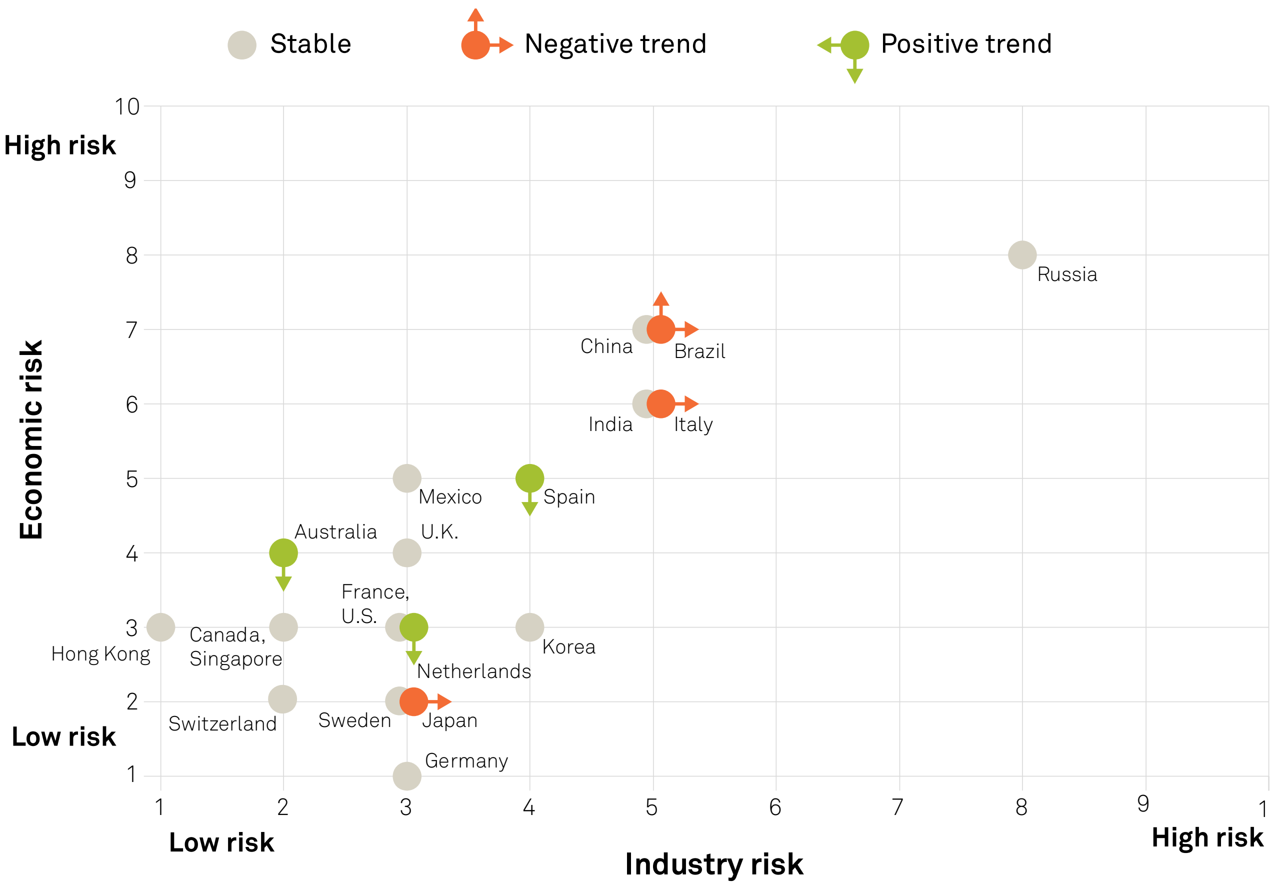
Key Takeaways

- We expect banks to face more market volatility in 2019 from policy uncertainty and the rollback of monetary easing.
- The credit cycle will turn sooner or later, putting the spotlight on the imbalances that have built up in some developed and emerging markets, even if improved balance sheet soundness in many banking systems should moderate the impact.
- The monetary policy shift could lead to an abrupt repricing of risks in financial markets and a correction in some housing markets (for example, Canada, Australia, China, Hong Kong, and New Zealand).
- Credit conditions remain broadly supportive for banks, but the threats posed by monetary policy normalization, trade tensions, and ongoing political risk are dragging down investor confidence and weakening economic momentum.
- Our assessment of recession risk in 2019 for the U.S. stands at 15%-20%. While credit conditions are generally satisfactory, we are watchful for any sign of rising problems in some segments (auto, credit card, commercial real estate, and leveraged loans).
- The economic momentum in Europe is weakening. Banks should be able to maintain sound balance sheets but will struggle to increase revenues and improve efficiency.
- The risk of a disruptive Brexit remains significant. British banks are the most vulnerable to the fallout, which would most likely lead to the U.K. economy contracting amid a domestic political crisis, leaving the property market and asset quality vulnerable.
- Concerns about fiscal sustainability in Italy could undermine confidence further, translate into higher borrowing costs, and constrain banks' progress.
- The climb in the U.S. dollar continues to stoke emerging market turbulence that could spread beyond Argentina and Turkey to other vulnerable countries. Capital flows to emerging markets are likely to remain under pressure in 2019.

Despite supportive credit conditions, the trade battle and monetary tightening are weakening investor confidence and economic momentum.

However, many banking sectors appear better equipped to face tougher times than a decade ago.

BICRA And Trends: Top 20 Global Markets



A BICRA (Banking Industry Country Risk Assessment) is scored on a scale from 1 to 10, ranging from the lowest-risk banking systems (group 1) to the highest-risk (group 10). Data as of Nov. 23, 2018.

Key changes in 2018

— BICRA on Spain **raised** to 4 from 5

— BICRA on Portugal **raised** to 6 from 7

— BICRA on Turkey **lowered** to 9 from 7

— BICRA on Malta **lowered** to 5 from 4

— BICRA on Lebanon **lowered** to 10 from 9

Key trend changes in 2018

— Industry Risk to **negative** from stable on Italy

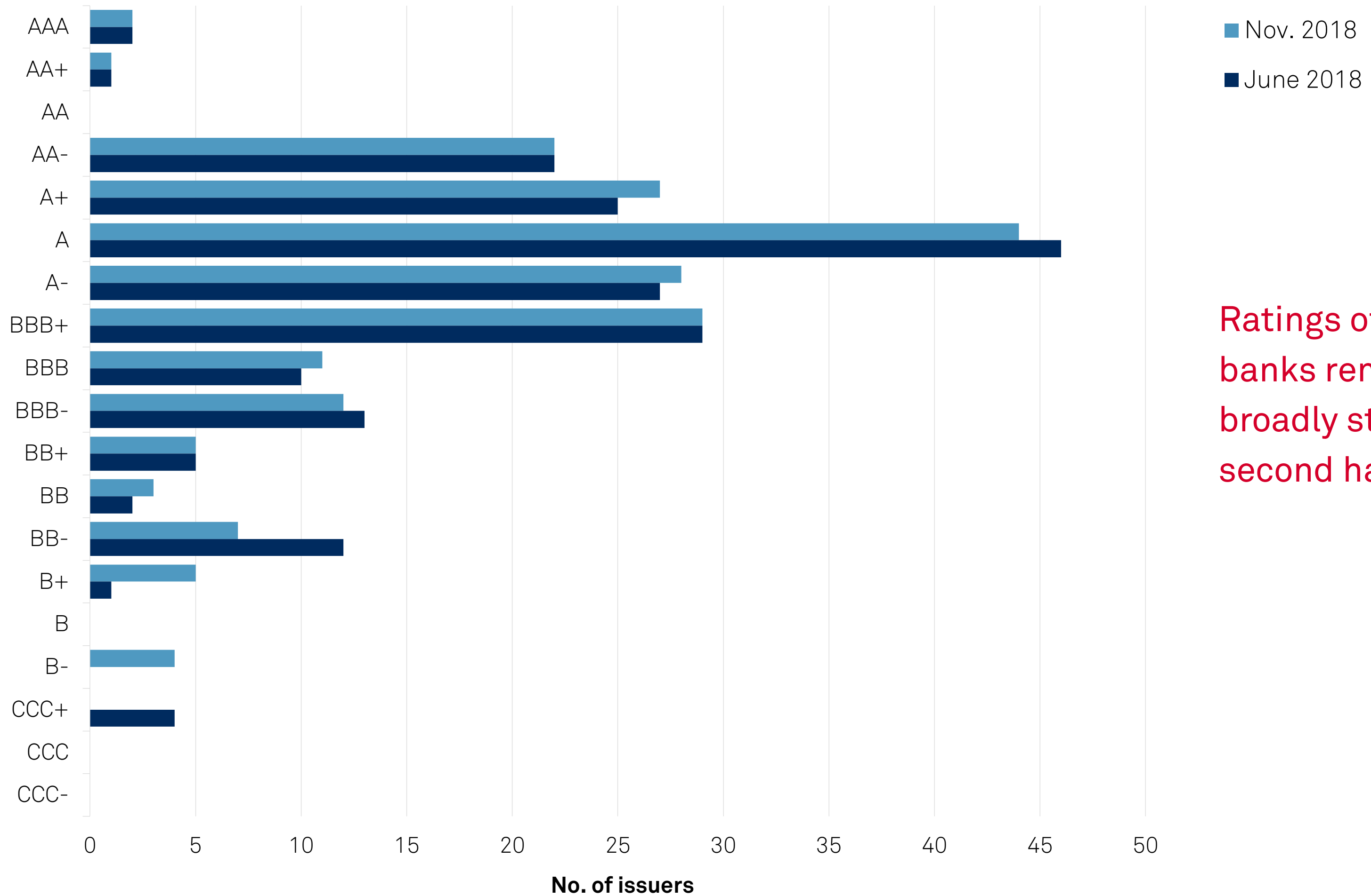
— Economic Risk to **stable** from negative on Hong Kong

— Economic Risk to **positive** from stable on Greece

— Economic Risk to **positive** from stable on Australia

— Economic Risk to **stable** from negative on Norway

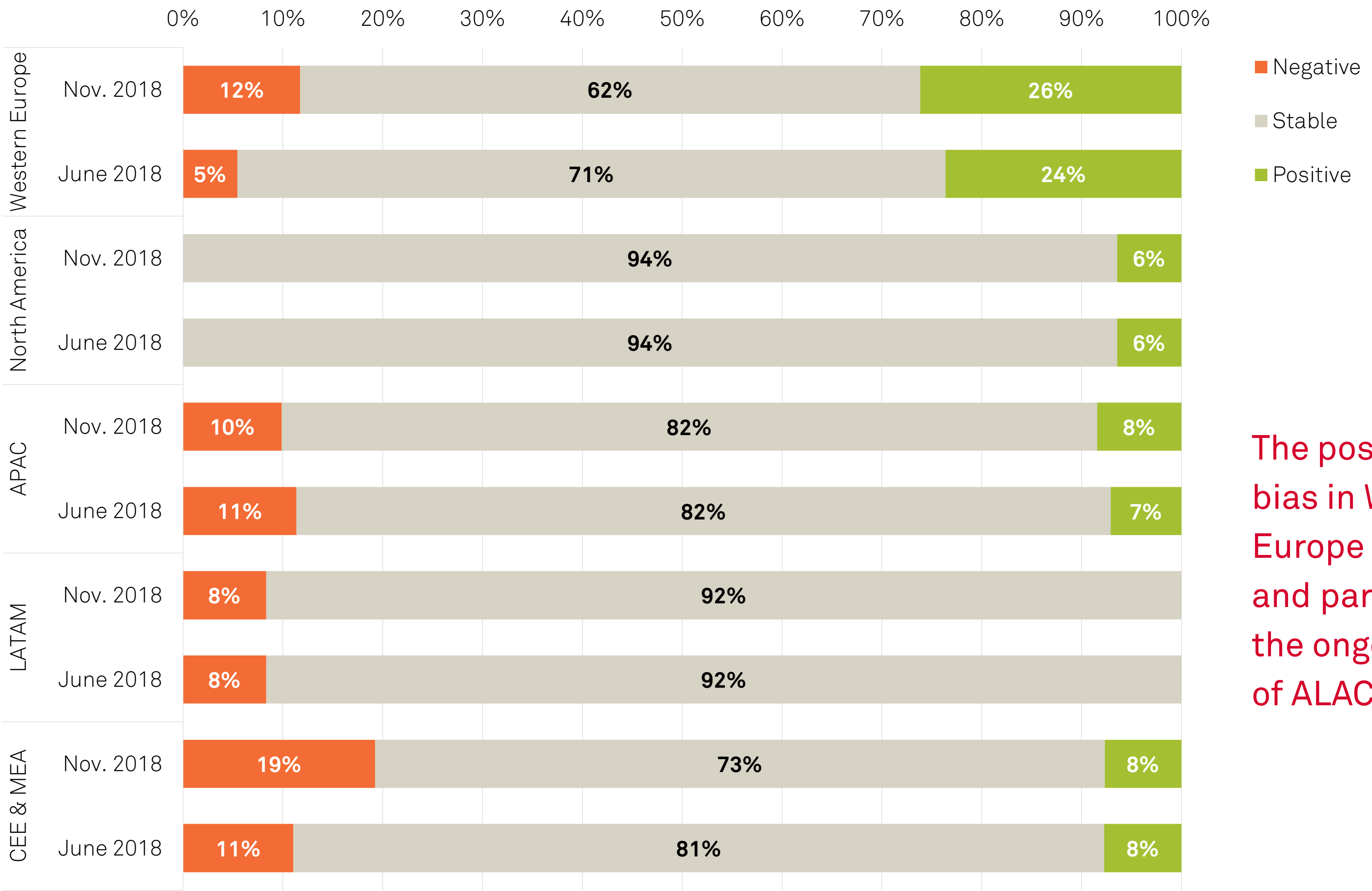
Ratings Distribution For The Top 200 Banks



Ratings of the top 200 banks remained broadly stable in the second half of 2018.

Operating company issuer credit ratings. Data as of Nov. 23, 2018. Source: S&P Global Ratings.

Bank Outlooks By Region



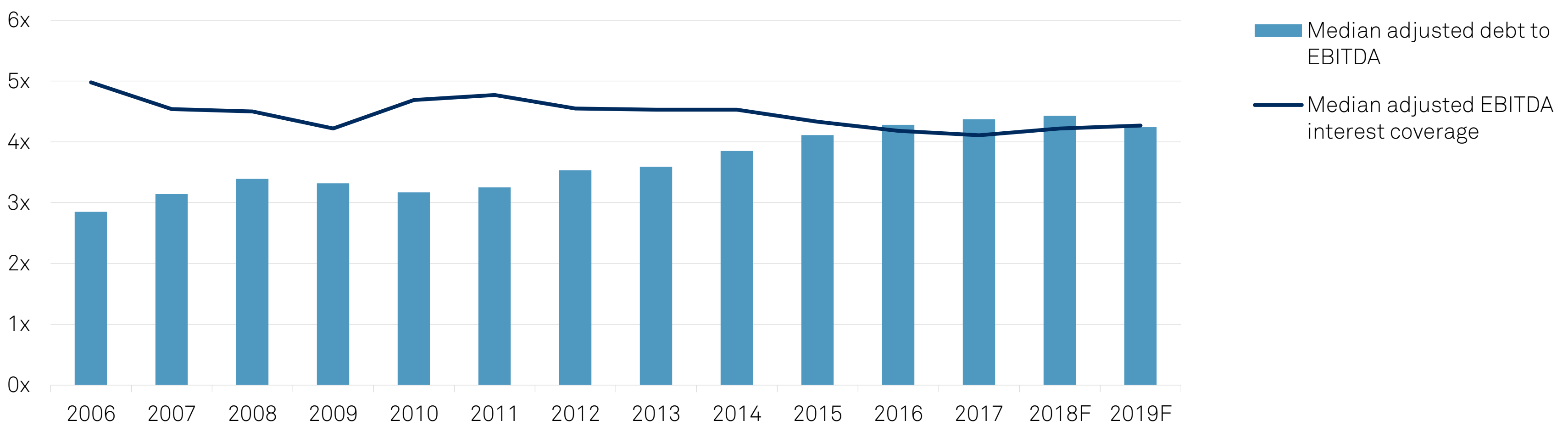
The positive outlook bias in Western Europe is reducing and partly reflects the ongoing build-up of ALAC.

Data as at Nov. 19, 2018. Based on the top 200 rated banks. Source: S&P Global Ratings.

Credit Conditions: U.S. And Canada

- The U.S. and China have escalated their tariff dispute and the two sides show little sign of forging a compromise. Still, we expect above-trend GDP growth (2.9% this year and 2.3% in 2019). The strong labor market, bullish consumer confidence, and favorable manufacturing sentiment bolster this view.
- Credit conditions in the U.S. and Canada remain broadly favorable, with the current credit cycle continuing its historic run. But the risk that the trade conflict will devolve into an all-out trade war outweighs the threats posed by monetary policy normalization, and the prospects for widening credit spreads for borrowers.
- We see rising corporate debt, the prospect that borrowing costs will rise faster than we forecast, and imbalances in Canada's housing market as the most significant risks.
- Declining average credit quality, along with a pick-up in U.S. leveraged lending and speculative-grade bond issuance since 2012, could amplify credit stresses if investor risk aversion unwinds still compressed credit spreads, or reduces share prices and market access to debt or equity financing.

U.S. Nonfinancial Corporate Median EBITDA Ratios



F--Forecast. Source: S&P Global Ratings.

US-China Trade Dispute Snapshot

April

1. China strikes back after solar panel & washing machine tariffs
China imposes about $3 bil. on U.S. Imports
- 15% tax on 120 U.S. Products including fruits, nuts, and steel pipes
- 25% tax on 8 U.S. Products including recycled aluminium & pork

2. And it Escalates
- US retaliates with a 25% tax on close to 1300 Chinese Products targeting $50 bil. worth of imports in response to IP theft
- China responds in kind with $50 bil. worth of U.S. Imports targeting 106 products including soybeans, autos, aircraft, and **a** chemicals

3. Trump not to be outdone
After China counter-tariffs, Trump announces another potential $100 bil. in tariffs

4. Tit for Tat
- U.S. bans exports to ZTE (resumed limited activity on 7/6)
- China returns with a 179% tariff on U.S. Sorghum

May

5. Talks begin
U.S. & China sit down to collectively work through Trade Issues

6. Cease Fire Reached
A “Cease-fire” has been reached between U.S. & China
- China removes hefty Sorghum tariff
- China lowers automobile tax from 25% to 15%

7. Trump Breaks Silence
U.S. announces it will move forward with $50 bil. of tariffs & limits on Chinese investment in U.S. Tech companies

8. China Extends Olive Branch
China offers but $70 bil. worth of U.S. products in an attempt to avoid proposed and future tariffs

June

9. U.S. Makes Good on Tariffs
U.S. approves it will move forward with $34 bil. of tariffs, by July 6^{th}. With another $16 bil. to follow, on possibly a revised product list

10. China Responds $ per $
China slaps $34 bil. in tariff’s starting July 6^{th}. With another $16 bil. to follow at a later date. Hitting such products as soybeans, electric/hybrid vehicles, and a variety of seafood and pork

11. And the Stakes are Raised
U.S. Trade Representatives have been directed to prepare a 10% tariff on $200 bil. worth of goods between U.S. & China

12. U.S. Limits Foreign Investment
The Treasury Department is working on rules to block firms with at least 25% Chinese ownership from buying companies with "industrially significant technology"

July

13. 25% is the New 10%
President Trump asks USTR to prepare a 25% tariff instead of the originally planned 10% on $200bn of imports

14. China Responds, but Cannot Match
China’s Ministry of Commerce proposes a additional tariffs on 5,207 products worth $60 bil. ranging from 5-10% hitting products such as meat, minerals, chemicals, machinery, furniture and auto parts

15. WTO to Referee
The Chinese Ministry of Commerce lodges formal complaint at the WTO against the US for its tariffs on solar panels, alleging that US tariffs have damaged China’s trade interests

16. Another Attempt At De-escalation
U.S. and Chinese mid-level representatives meet for the first time since early in the trade skirmish. Discussions end with no major breakthroughs.

Aug.

17. Trump Ups the Ante
After the public comment period for $200 bil. round of tariffs, Trump threatens an additional round of tariffs on $267 bil. worth of goods. Which would potentially bring the total amount of tariffs imposed on China to $517 bil.

18. China Promises “Countermeasures”
The Chinese Foreign Ministry responds to the additional tariff announcement on $267 bil. worth of goods by stating “...Chinese side will inevitably take countermeasures to resolutely protect our legitimate rights”

19. U.S. Tariffs Hit $250 bil.
The U.S. makes good on its threat to impose tariffs on another $200 bil. of Chinese imports. The tariff rate of 10% from Sept. 24, 2018 will rise to 25% on Jan. 1, 2019 unless the two countries come to a compromise

20. China Delivers on Retaliatory Tariffs
China announced a $60 bil. retaliatory tariff of 5-10% on 5,207 U.S. goods. But may have to consider other tactics in order to match effective U.S. tariff measures

Sept.

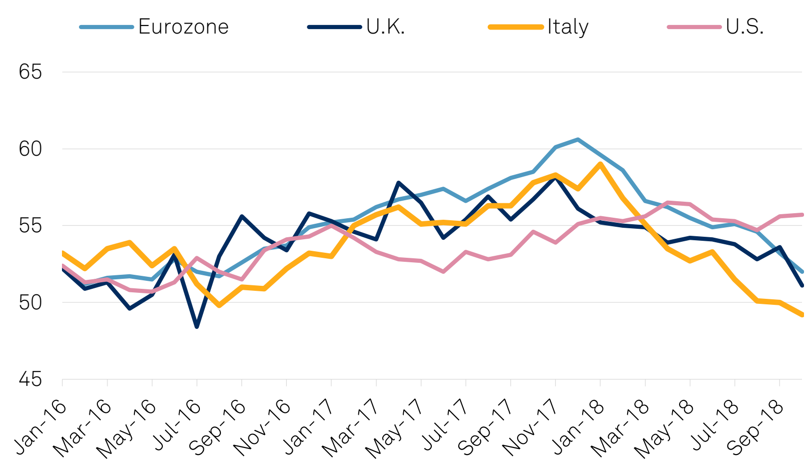
21. New Round of Tariffs Go Into Effect
China & U.S. exchange new round of tariffs, bringing total enacted to $250 bil. (U.S.) and $110 bil. (China). Chinese government call off talks with U.S. as consensus grows in Beijing that substantive discussions will only be possible after U.S. midterm elections

22. U.S. Continues Tariff Pressure
The US is reportedly prepared to announce tariffs on all remaining Chinese products if talks between Trump and Xi at the G20 in Argentina are not successful

Credit Conditions: Europe

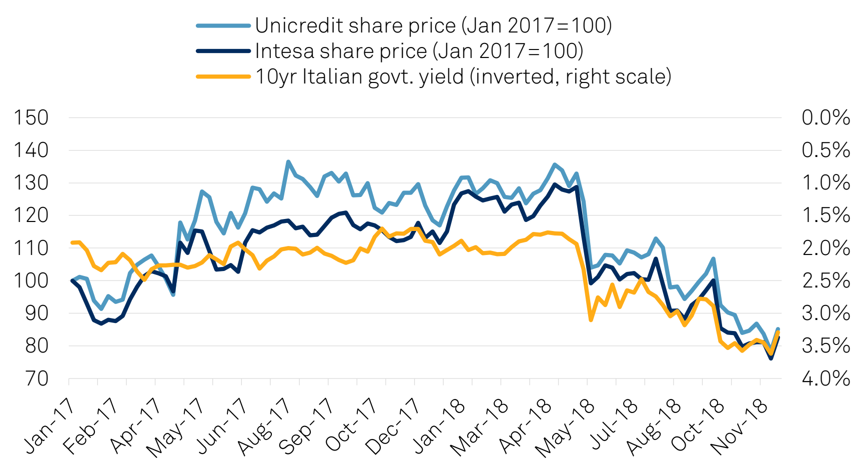
- The Eurozone economy has shifted down a gear since the start of the year, but capacity pressures remain high. Against this backdrop, we expect the European Central Bank (ECB) to start with the gradual normalization of its monetary policy, with two rate rises per year from 2020, after an initial one in the second half of 2019. We expect the euro to remain at its current level until mid-2019 in a context of political uncertainty and rising monetary policy divergence with the U.S.
- Credit conditions are tightening somewhat in the U.K. The risk of a disruptive Brexit remains significant, despite the U.K. and the EU having reached a draft withdrawal agreement. In addition, the Italian government maintained its expansionary budget in a clear challenge to the European Commission, which is feeding market volatility.
- Eurozone private-sector credit conditions remain benign, encouraging reasonable loan demand.
- Mainstream political parties continue to be challenged from all sides. With their sights set firmly on the European parliamentary elections in May 2019, a sizable vote for nationalist parties could put the brakes on any remaining momentum toward a closer union.

EU Manufacturing PMIs Diverging From U.S. Recently



PMIs--Purchasing manager indices. Sources: Markit, Thomson Reuters Datastream.

Italian Banks Shares Remain Sensitive BTP Bond Yields



Source: Thomson Reuters Datastream.

Credit Conditions: APAC

- Credit conditions in Asia-Pacific have worsened, with financing conditions tighter and macroeconomic sentiment weaker. The continuing China-U.S. trade war and emerging markets currency sell-down is darkening investors' mood.
- Spillover from the emerging market crises in Argentina and Turkey is pressuring local currencies, notably the Indian rupee and Indonesian rupiah.
- Trade interruption risk continues to rise. Emerging market contagion risk has returned in the form of currency depreciations, highlighting asset price volatility and liquidity pullback risks. While China's debt risk is mostly stable, the government's efforts to deleverage the system have slowed as the need to maintain rapid economic growth is high. Positively, Korean geopolitical tensions have eased.
- As anticipated, financing conditions in emerging Asia are facing headwinds going into 2019.
- While economic activity is still solid, leading indicators point to moderation ahead with a softening in new orders and household and business confidence.

Indian, Indonesian Currencies Under Pressure

Sources: Bloomberg, S&P Global Ratings.

China Credit Spreads Widen

Yield gap between five-year Chinese government bonds and medium-term notes rated AA- (domestic ratings)

Sources: CEIC, S&P Global Ratings.

Credit Conditions: LATAM

- We expect challenging credit conditions to carry on in 2019 due to trade tension, continued rate hikes in the U.S., and commodity price trends. While domestic political risks have dissipated in some countries, challenges remain for some new administrations.
- We expect risks in the region to remain elevated and potentially worsen in 2019. While positive, global economic growth is trending downward.
- We expect financing conditions to continue weakening as interest rates in the U.S. increase and other developed countries consider tighter monetary policies. On top of more restrictive external conditions, investor sentiment toward the region might be undermined by political developments over the next months. Also, appetite for emerging-market debt remains fragile, demanding higher risk premiums, especially from issuers in the 'B' rating category.
- Rising interest rates and falling currencies, stemming from weakening external conditions, will continue pressuring issuers in the region.

Latin America's GDP Growth

			Base Scenario			
	2016	**2017**	**2018**	**2019**	**2020**	**2021**
Argentina	-1.8	2.9	-2.5	-0.8	2.5	3.0
Brazil	-3.4	1.0	1.4	2.4	2.5	2.6
Chile	1.2	1.6	4.0	3.3	3.0	3.0
Colombia	2.0	1.8	2.6	2.9	3.0	3.0
Mexico	2.6	2.3	2.2	2.2	2.4	2.5
Panama	5.0	5.4	4.0	5.0	5.0	5.0
Peru	4.1	2.5	3.6	3.8	3.8	3.8
Uruguay	1.7	2.7	2.1	2.2	2.7	2.9
Venezuela	-12.0	-10.0	-10.0	-5.0	2.0	2.5
LATAM	**-1.1**	**1.1**	**0.9**	**1.7**	**2.6**	**2.7**
LATAM ex. Venezuela	**-0.4**	**1.8**	**1.6**	**2.2**	**2.6**	**2.8**

Note: the LatAm GDP aggregate forecasts are based on three-year average (2014-2016) PPP GDP weights. Our GDP numbers are based on seasonally-adjusted series when available. Source: S&P Global Ratings.

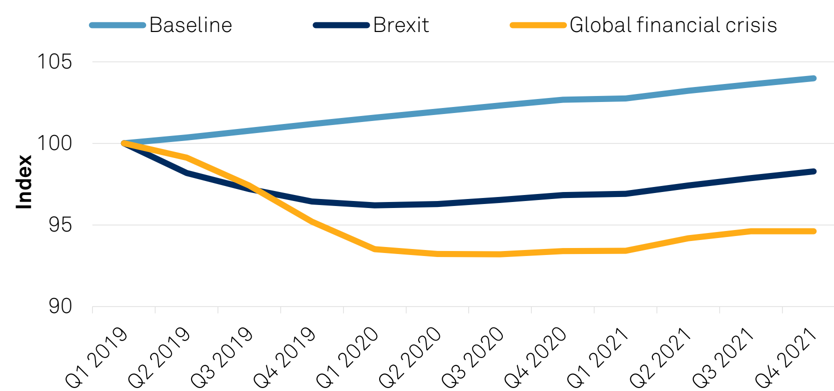
Impact Of A No-Deal Brexit

- While the EU and the U.K. have reached an agreement on the terms of the U.K.'s withdrawal from the EU and on a framework for their future relationship, there remains a significant risk that the U.K. parliament will not approve the deal.
- In that scenario, unless other avenues toward an agreement opened up, the U.K. would leave the EU with no deal in place.
- Our no-deal scenario posits a moderate U.K. recession, with GDP falling by 2.7% over two years, and a partial recovery thereafter.
- U.K. banks will likely be the most vulnerable in a no-deal Brexit, but their earnings and balance sheets would provide a material cushion.
- Other open economies like Ireland, Belgium, or Netherlands could also feel the impact of no deal, but we expect those countries' banks to better accommodate its adverse consequences.
- A no-deal Brexit that leads to a severe economic downturn in the U.K. would likely result in a deterioration of U.K. banks' asset quality and earnings. More immediately, U.K. banks could face constrained and/or more expensive access to wholesale funding.

Key Figures From The No-Deal Scenario

GDP	Unemployment	Households lose	Inflation peaks at	House prices down
5.5%	7.4%	£2,700	4.7%	10%
below our baseline forecast by 2021	by 2021	in income per year 2019-2021	in mid-2019	by 2020

A No-Deal Brexit Would Be 60% As Damaging To The U.K. Economy As The Global Financial Crisis

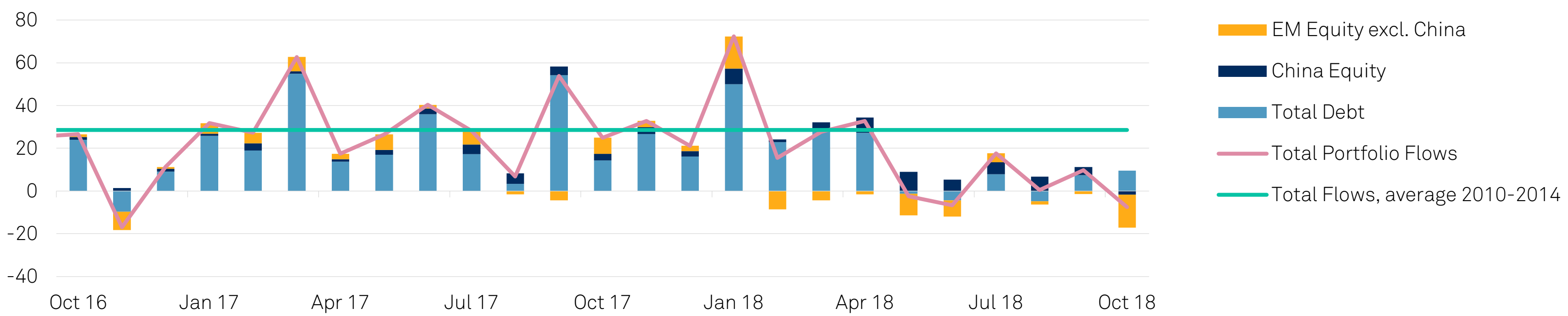


Note: Index=100 in quarter before the shock. GDP index has been transformed for the global financial crisis so that is consistent and can be compared with our baseline forecast. Sources: ONS, S&P Global Economics & Research.

Overview Of Emerging Markets

- Rising U.S. interest rates, a stronger U.S. dollar, and tightening of monetary policies have led to increased volatility for some emerging market (EM) currencies and triggered episodes of capital outflows. This trend will continue in 2019.
- About 20% of our BICRA economic or industry risk trends on EMs are negative. The most common reasons are the build-up of imbalances, political risk, and sharp slowdown in some economies.
- China represents the largest global threat due to its disproportionate size (at 15% of world's GDP). Although we don't envisage a hard landing, a material deterioration would hurt global trade, economic growth, and commodity prices.
- The deterioration in Turkey and Argentina weakened some EM currencies (for example, those of India, Malaysia, and South Africa) but risks remained contained so far.
- The high proportion of nonfinancial sectors' debt in foreign currency in many EMs (Turkey, Indonesia, for instance) is a key risk.
- Escalating trade tensions might trigger lower commodity prices (a trend that recently started), hurting certain EMs whose export revenues show a concentration on commodities (for example, GCC countries, Russia, Nigeria).
- Geopolitical tensions and economic sanctions will likely continue hurting a number of EM banking sectors, limiting access to external capital markets, long-term funding, and pushing up funding costs (Russia, Qatar, and Turkey, for example).
- The presidential elections in Brazil, Mexico, and Colombia removed only part of the uncertainty. For Brazil, markets reacted positively but the new administration needs to rapidly pass crucial unpopular reforms to reverse negative trends.
- Banking regulation in EMs is converging toward international standards but governance and transparency remain a weak spot.

Net Non-Resident Portfolio Flows to Emerging Markets



Sources: IIF, S&P Global Ratings calculations.

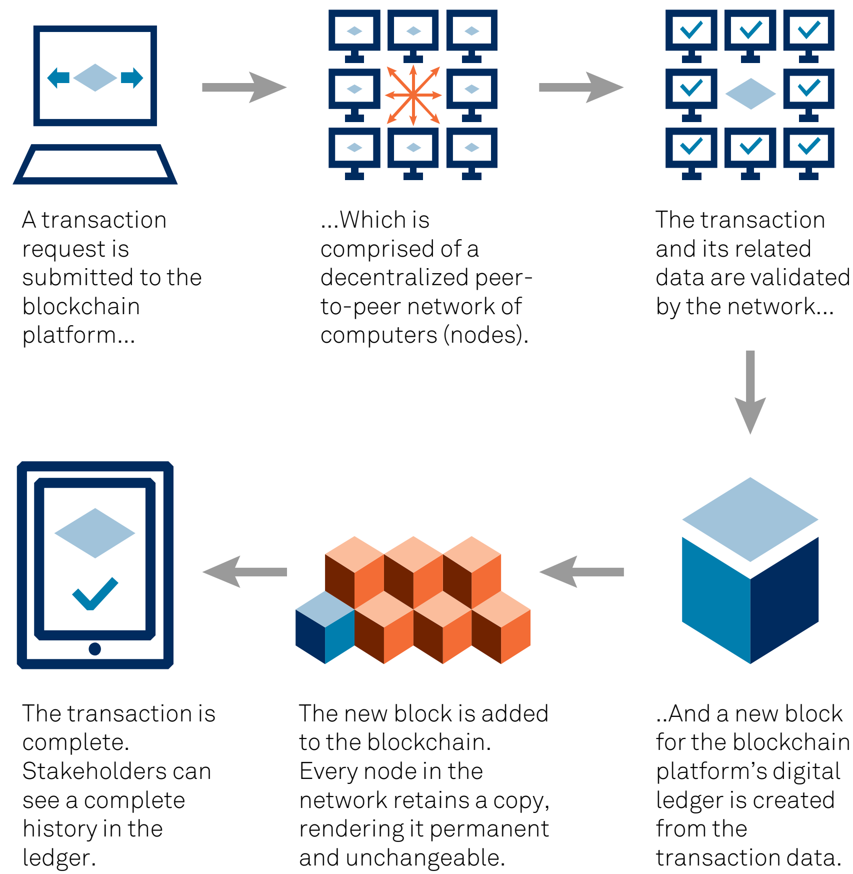
Regulation / Anti-Money Laundering

- The high tide of prudential regulation tightening was reached with the finalization of Basel III in December 2017. Instead, we see now the risk of delayed or uneven implementation of the agreed global standards.
- We also see a risk of fragmentation or lessening cooperation between supervisors around the globe – against a backdrop of simmering anti-globalization sentiment. This could lead to a less effective response to potential crises when the cycle turns.
- Progress around TLAC (Total Loss-Absorbing Capacity) and MREL (Minimum Requirements for owned funds and Eligible Liabilities) continues with resolution authorities expected to publish binding bail-in buffer requirements for additional European banks in the first quarter of 2019. This will further catalyze banks to issue loss-absorbing instruments.
- Spreads are widening, especially on nonpreferred debt, due to a normalization in risk appetite, adding further headwinds to interest margins in Europe. An increasing share of the new debt being issued is loss-absorbing and therefore rated below the issuer credit ratings.
- A series of bank money-laundering cases in some European countries (Latvia, Denmark, Malta, Estonia, for example) is likely to push regulators to strengthen their regulation and supervision. At this stage though, there are few reasons to be optimistic that such problems will not recur, at least in the near-to-medium term. In addition, the cost (fines, settlements, licensing restrictions) of regulatory noncompliance is already high for cases pursued by the U.S. authorities, and appears to be rising in Europe.
- The U.S. regulatory reform bill passed in May 2018 will mainly lessen regulation on regional and community banks--potentially allowing for weaker financial management and greater risk-taking.
- However, we believe the proposals, while incrementally negative for creditors, do not materially weaken overall banking sector stability, in large part because they leave regulation on the GSIBs mostly unchanged.

Fintechs: Challengers Or Catalysts?

- We expect partnerships between banks and fintechs to grow and strengthen.
- We see more and more banks embracing opportunities to onboard convenient solutions from outside product providers to enhance their value chain.
- That said, fintechs will increasingly disrupt the revenue bases of banks, especially more lucrative activities subject to lower barriers to entry (for example, payment services).
- Investments in digital transformation will generally outweigh related cost savings in the near term, at a time when banks in Europe and Japan still deliver subpar returns.
- The implementation of PSD2 in Europe is forcing banks to provide access to valuable customer data to third-parties, but industry leaders are increasingly using the API (application programming interface) bridges as platforms to enhance client experience.
- Meanwhile, we expect a further expansion of global tech titans, mainly from China and the U.S., into business areas of traditional banks and beyond payments.
- Regulations and questions about data privacy may in some cases slow down the expansion of the tech titans into certain traditional banking activities.
- This new competition will be a catalyst for banks to accelerate process and product innovation, and leverage the benefits from big data and blockchain technology.

How Blockchain Enables Transparent Tracking Of Assets



Sources: Blockgeeks, S&P Global Ratings.

North American Banks

Key Expectations

— Some U.S. banks may further benefit from rising interest rates, but we expect more banks to begin reporting net interest margin contraction.

— The May 2018 legislative changes on regulation and the Fed's recent proposal to tailor regulation based on asset size did not affect our ratings on U.S. banks but could lead to greater risk for individual banks.

— The proposal to revise regulatory capital requirements for large banks (the stress capital buffer) could force some of the U.S. largest banks to boost capital.

— For Canadian banks, we expect operating performance to continue to improve from domestic, U.S., and international businesses.

Key Assumptions

— We expect the Fed to raise rates in December 2018 and three more times in 2019, and GDP growth in both the U.S. and Canada to remain solid.

— Loan growth is likely to continue at a low- to mid-single-digit pace.

— Credit losses have likely bottomed out and may gradually increase in 2019.

Key Risks

— Rising interest rates could further hurt market valuations and eventually asset quality. Also, the cost of deposits could rise more quickly than anticipated.

— Corporate credit quality, particularly in leveraged lending, could deteriorate after several years of significant growth.

— In Canada, a decline in home prices could lead to higher loan losses.

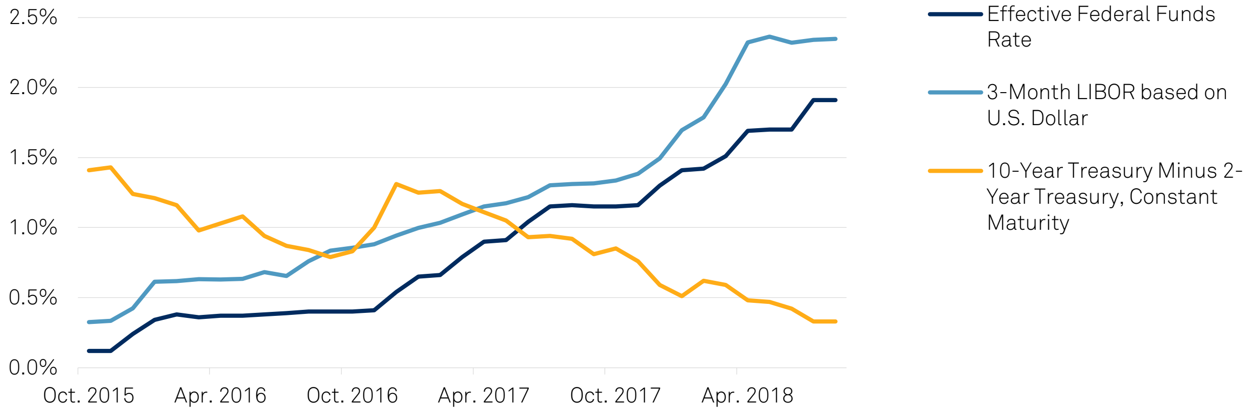
Outlook For U.S. Banks Is Slightly Positive

Worsening | | Neutral | | Improving

Revenues	Net interest income is likely to rise moderately on modest loan growth with incremental interest margin improvement, at least for some banks. However, the benefits of rising rates will diminish. Fee income will depend on capital markets activity, market valuations, and mortgage volumes.
Expenses	Expenses will likely keep growing at a limited pace. Banks will continue to contain costs by consolidating branches, containing head count, and growing digitalization. However, investments in technology will be somewhat of an offset.
Profitability	Profitability may improve incrementally due to some increase in revenues and limited expense growth. However, gains will not be as significant as in 2018, which benefited from reduction in U.S. corporate tax rates. An eventual rise in provisions may also limit profitability.
Credit Quality	Rising rates will likely ultimately hurt credit quality, which has been very good in recent years. We expect nonperforming assets and net charge-offs to rise gradually in 2019. Specific areas of potential risk include leveraged, auto, credit card, and pockets of commercial real estate loans.
Capital	Capital ratios have likely peaked, particularly for regional banks. However, some GSIBs may have to increase their ratios somewhat depending on the finalization of the Fed's proposed stress capital buffer, as well as the 2019 Comprehensive Capital Analysis and Review (CCAR) results.
Funding & Liquidity	The ongoing rise in interest rates is likely to increase banks' asset sensitivity. We expect more depositors to shift funds out of non-interest and low-yield accounts into higher-yield deposit accounts and money market funds. The Fed's actions to shrink its balance sheet should contribute to this trend.

Margins May Begin To Stagnate In 2019

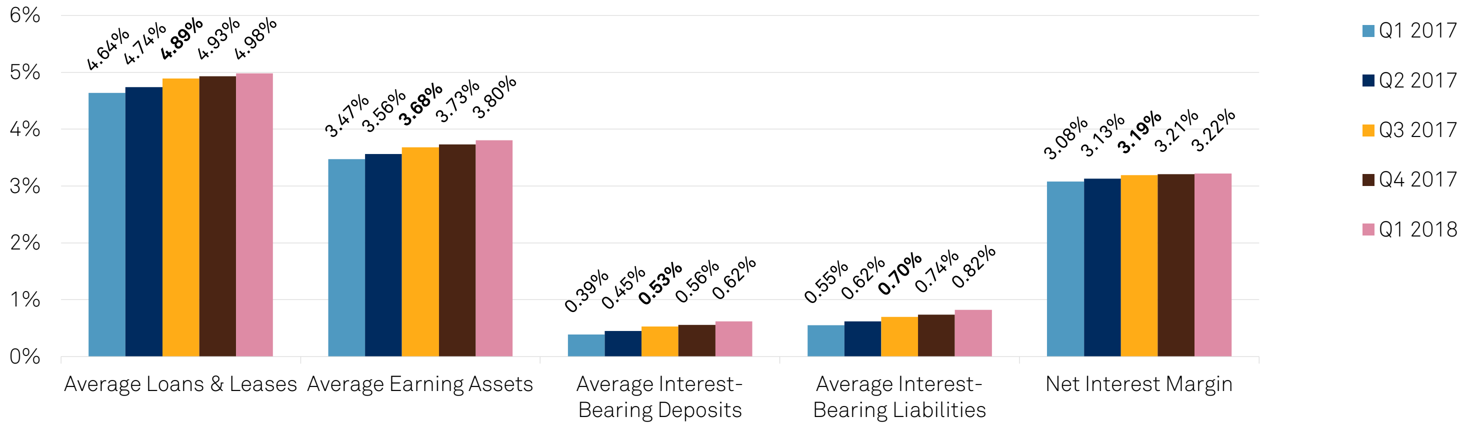
Benchmark Rates and Spreads



Source: S&P Global Ratings.

S&P Global Ratings expects the cost of deposits to rise more significantly after the Fed raises rates in December 2018 and three times in 2019.

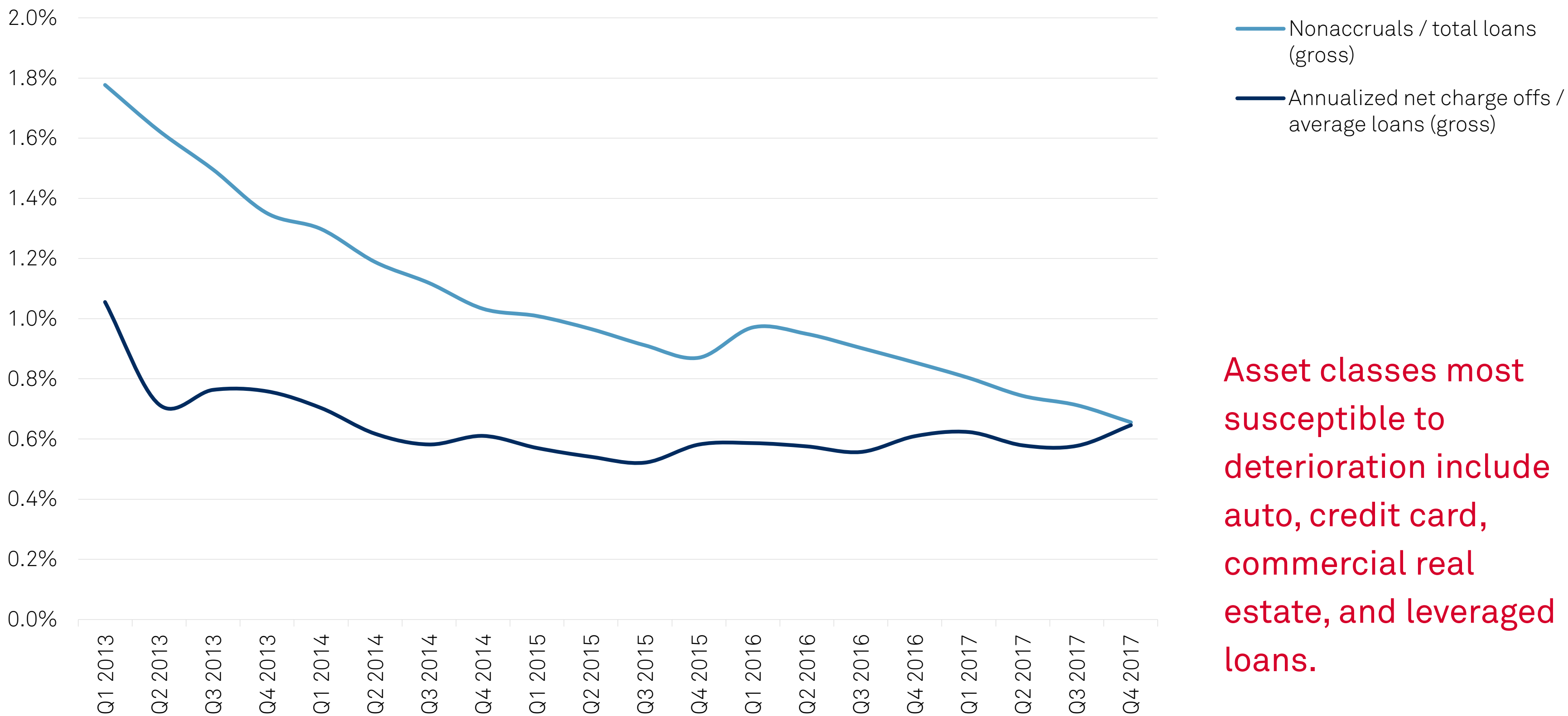
Yields and Costs: All Commercial Banks



Sources: Regulatory filings, FRED.

Asset Quality Is Excellent For U.S. Banks

NPAs and NCOs: All FDIC



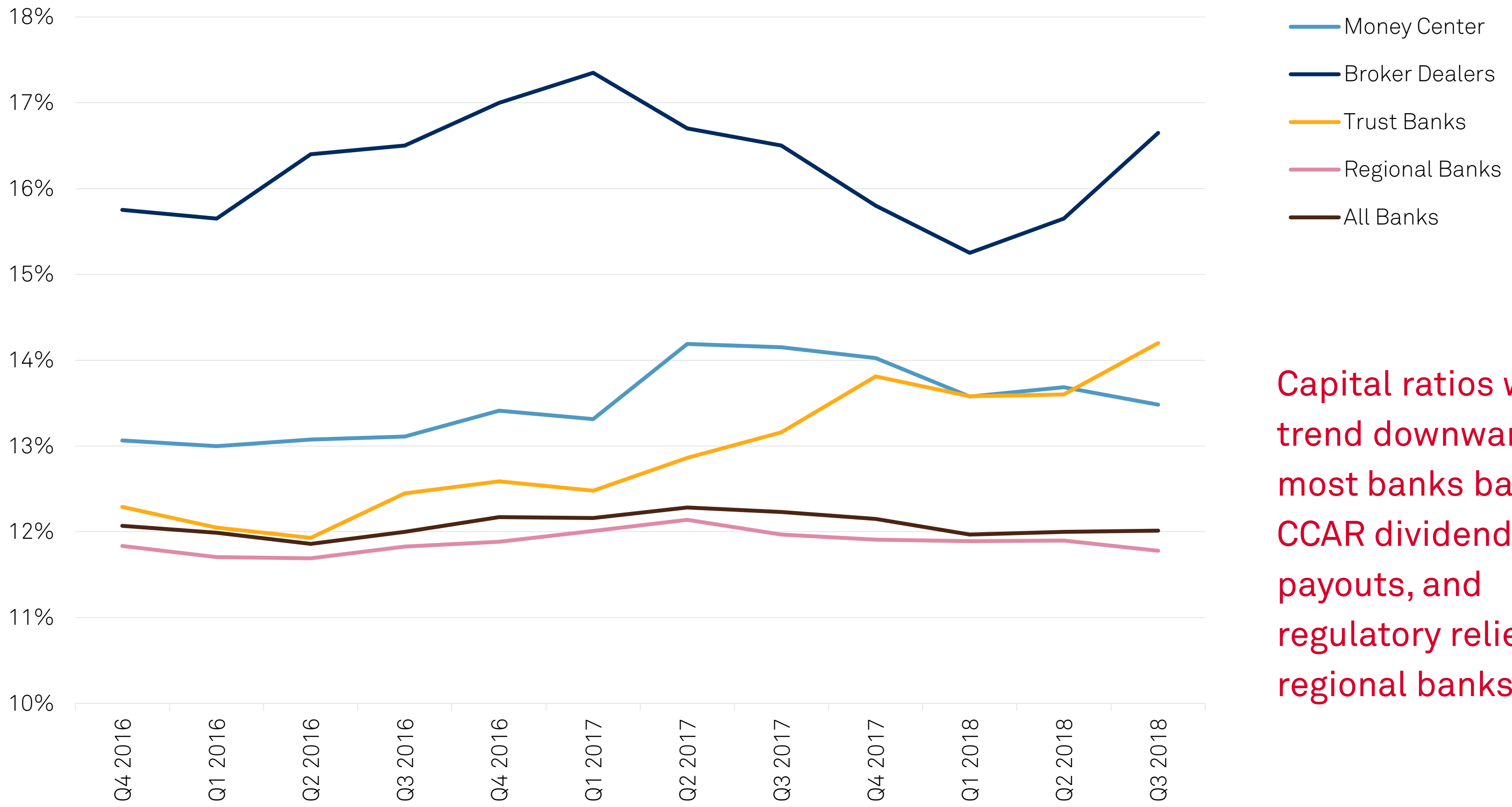
Asset classes most susceptible to deterioration include auto, credit card, commercial real estate, and leveraged loans.

Note: Adjusted Nonperforming Assets include nonaccrual loans, loans 90 days past-due, restructured loans, and OREO (Other Real Estate Owned). All FDIC (Federal Deposit Insurance Corporation) results estimated by aggregating Call Report data. NCO--Net charge offs. NPAs--Nonperforming assets.

Sources: S&P Global Ratings, S&P Global Market Intelligence, regulatory filings.

Capital Levels Likely To Decline

Median Tier 1 Ratio



Capital ratios will likely trend downward for most banks based on CCAR dividend payouts, and regulatory relief for regional banks.

Note: Transitional calculations. CCAR--Comprehensive capital analysis and review.

Sources: S&P Global Ratings, bank regulatory filings, S&P Global Market Intelligence.

European Banks

Key Expectations

- We expect a more balanced mix of upgrades/downgrades in 2019. We anticipate relatively stable balance sheets, modest new lending, benign asset quality with some progress in nonperforming assets' reduction in the periphery, stable capitalization, and subpar profitability.
- Authorities will continue working to enhance bank resolvability and systemic banks will continue to build their buffers.
- Potential divestments of government stakes in banks rescued during the crisis and some domestic consolidation, but not yet cross-border mergers.
- Potential for episodes of market turbulence, which could lead to increased funding costs for some banks.

Key Assumptions

- Brexit will not be disruptive.
- Economic growth will converge to its potential rate, but will remain generally supportive of banking activity.
- The ECB monetary policy shift will be gradual, allowing banks time to adjust.

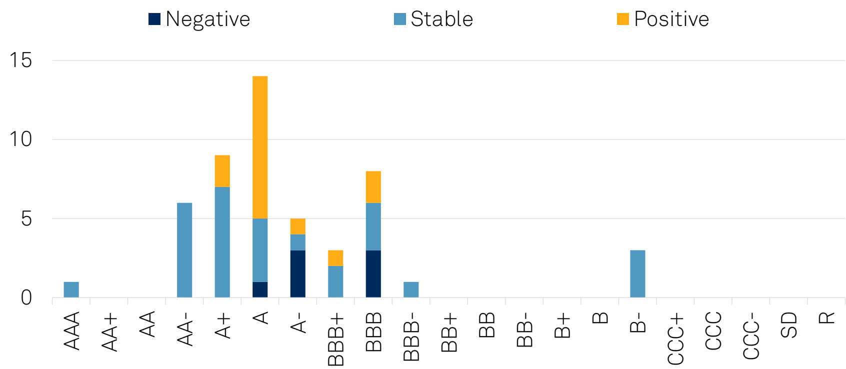
Key risks

- A disorderly Brexit with a likely negative impact on the economy.
- An ongoing turmoil in Italy, which could result in higher funding costs for the private sector (including banks), slow economic growth, and constrain banks' progress in their recovery, which is just half-way through.
- A reversal of economic momentum that would challenge our expectations of benign asset quality and slow the ongoing reduction of legacy problematic assets in the periphery, complicate the repositioning of banks' business models, and stagnate banks' profitability at low levels.
- An abrupt correction of the fixed-income markets, hitting capital through the mark-to-market of securities portfolios, reducing lending, and increasing funding costs for banks.

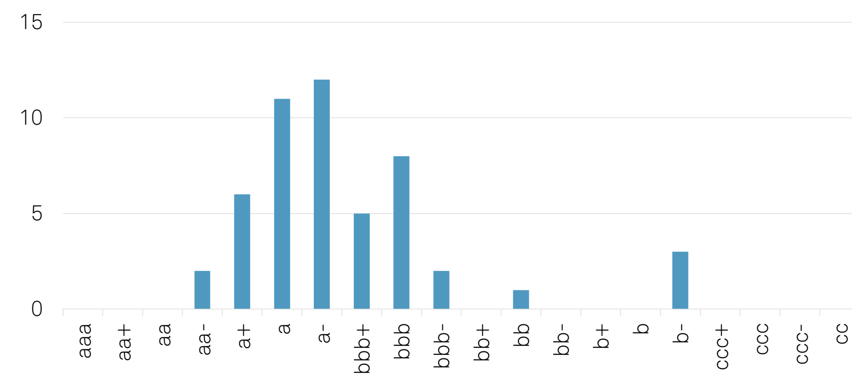
European Banks: More Mixed Rating Activity Expected In 2019

Rating Distribution: Top 50 European Banks

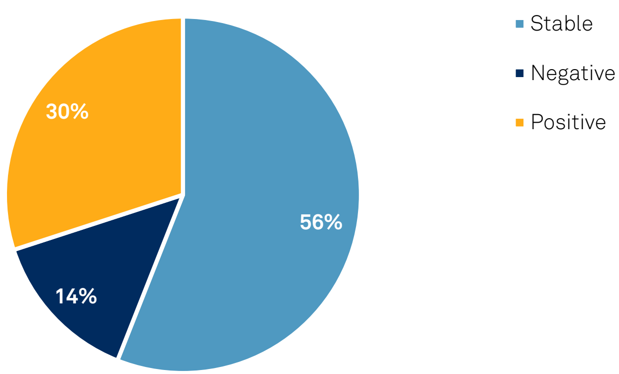
Operating company issuer credit ratings



SACP Distribution: Top 50 European Banks



Outlook Distribution: Top 50 European Banks

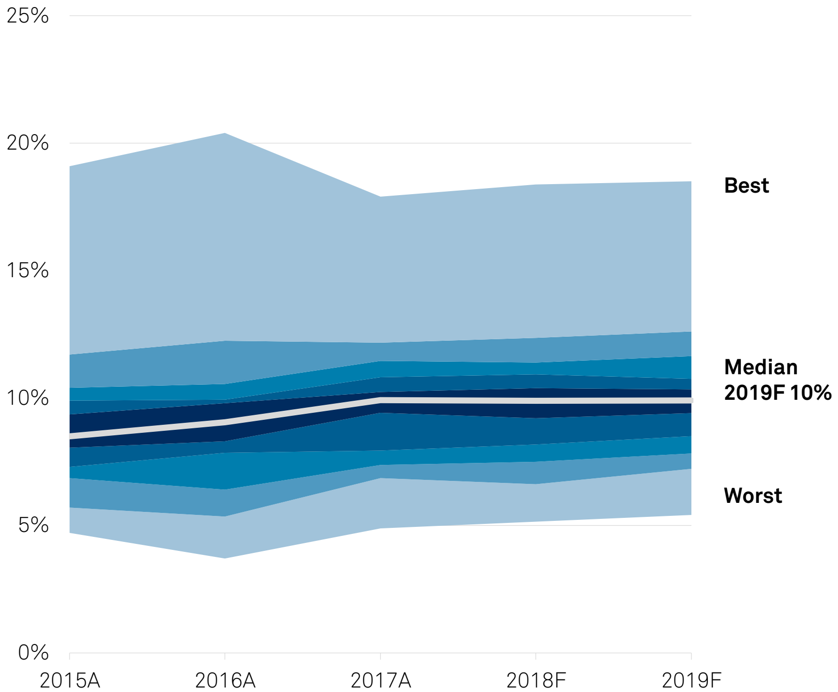


All data as at Nov. 19, 2018. Source: S&P Global Ratings.

- For six of the 15 positive outlooks, only the ICR has uplift potential.
- Expectations of a build-up of capital or MREL explain seven of the 15 positive outlooks.
- The remaining eight relate to progress in restructuring or easing of economic risks.
- The entities carrying a negative outlook are Italian banks, Danske Bank, Commerzbank, Volkswagen Bank, and BBVA.

Despite Loosening Momentum, Economic Growth Should Remain Supportive of Stable Capital and Benign Asset Quality

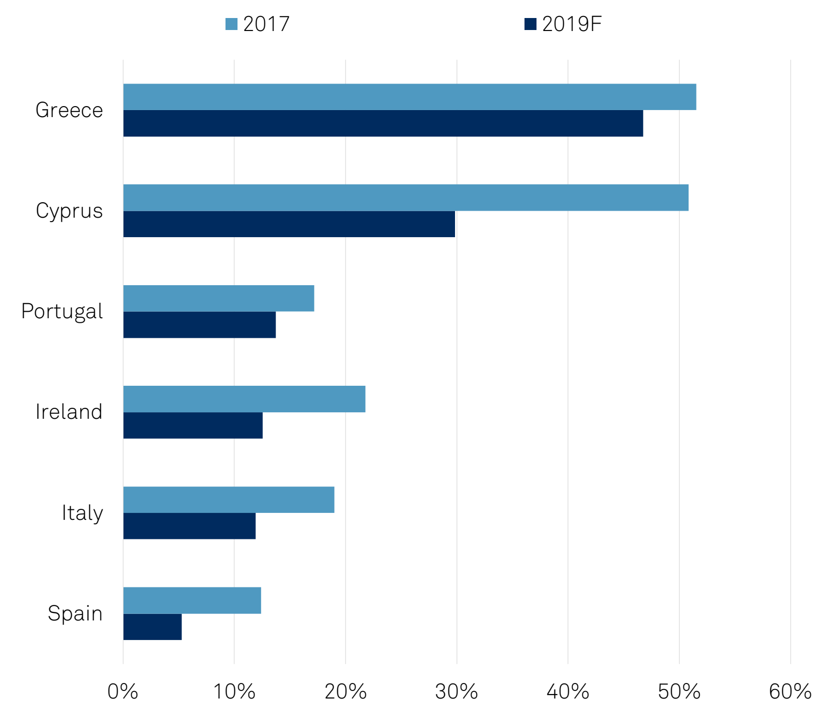
RAC For Top 50 European Banks



Each band depicts the distribution of 10 banks, with the darkest shade being the 10 closest to the median and then each lighter shade being the next 10 further away. Data as of Nov. 2018. A--Actual. F--Forecast.

Source: S&P Global Ratings.

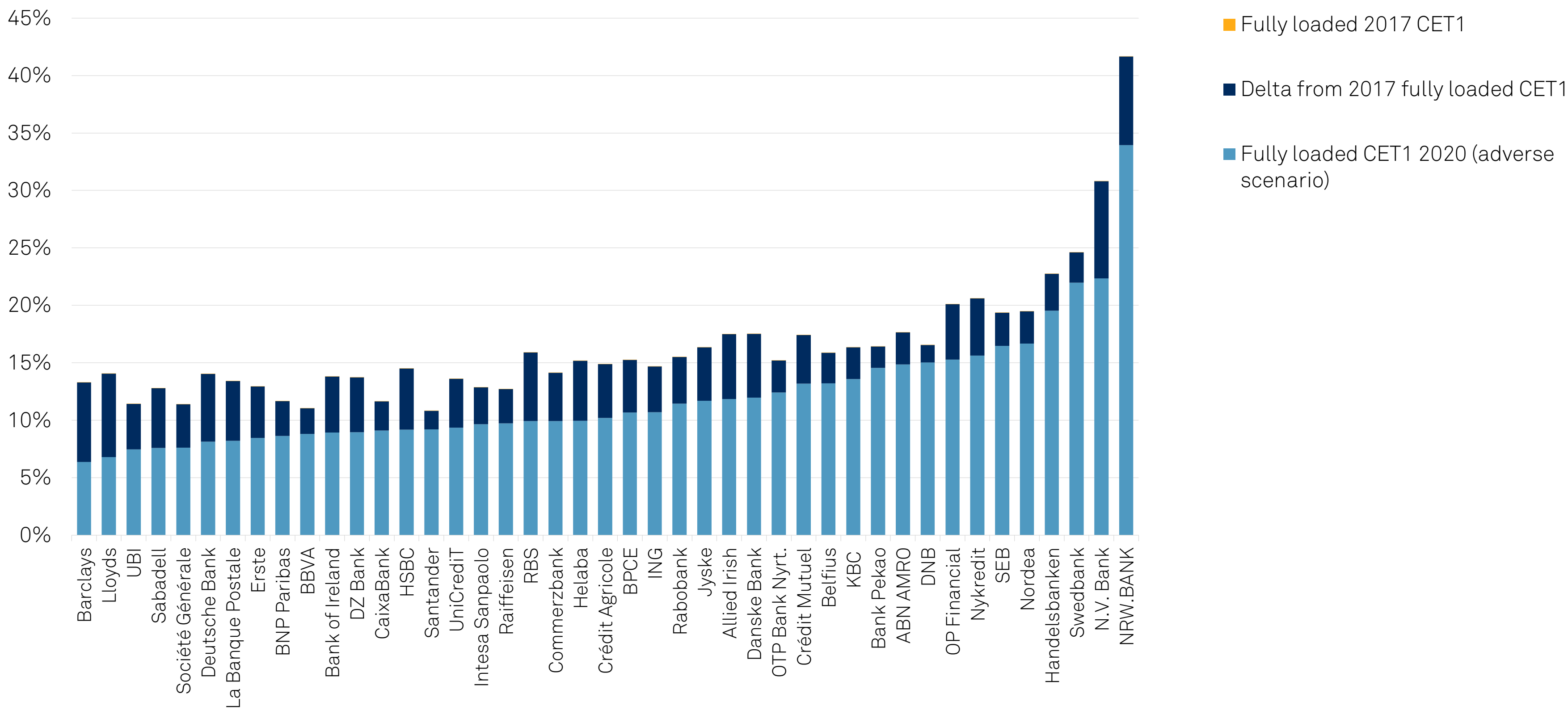
Expected Evolution Of Domestic Problem Loans/Loans



Source: S&P Global Ratings.

EBA Stress Test Underscores Increased Resilience Of European Banks

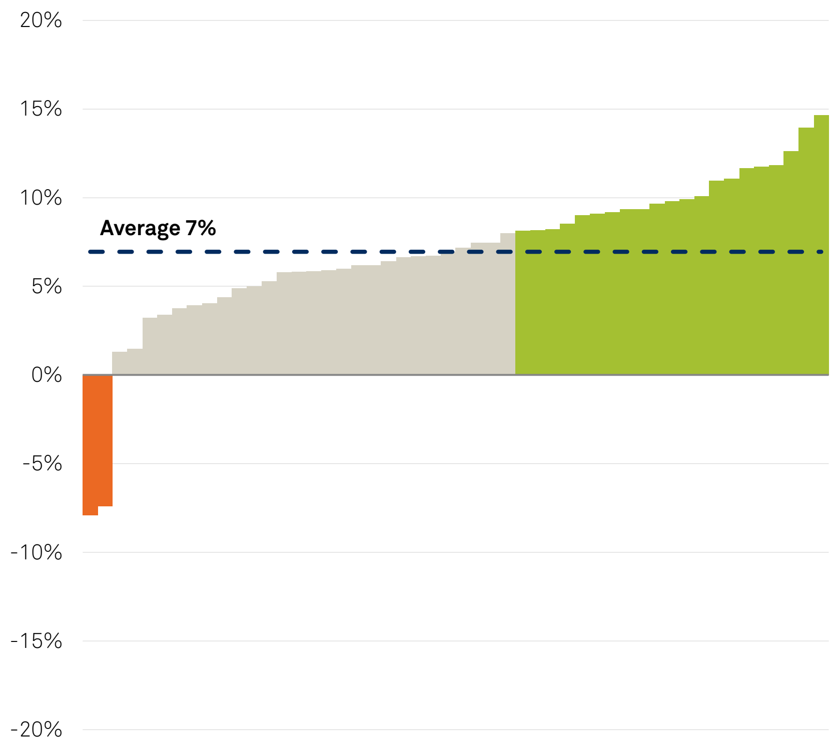
Results of the 2018 EU-Wide Stress Test Performed By The EBA



European Banking Authority (EBA) stress test results published on Nov. 2, 2018

Profitability Will Improve But Remain Subdued, Partly Explaining Weak Valuations

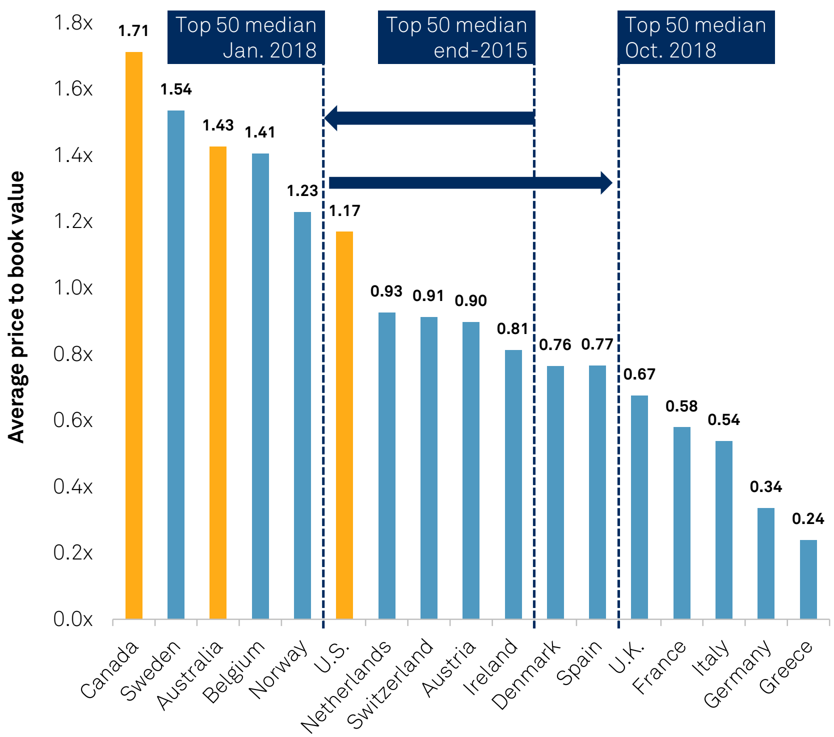
European Top 50 Banks: S&P Forecast of 2019 Return on Equity



Data as of Oct. 31, 2018.

Source: S&P Global Ratings.

Price to Book Ratios for Largest Banking Sectors

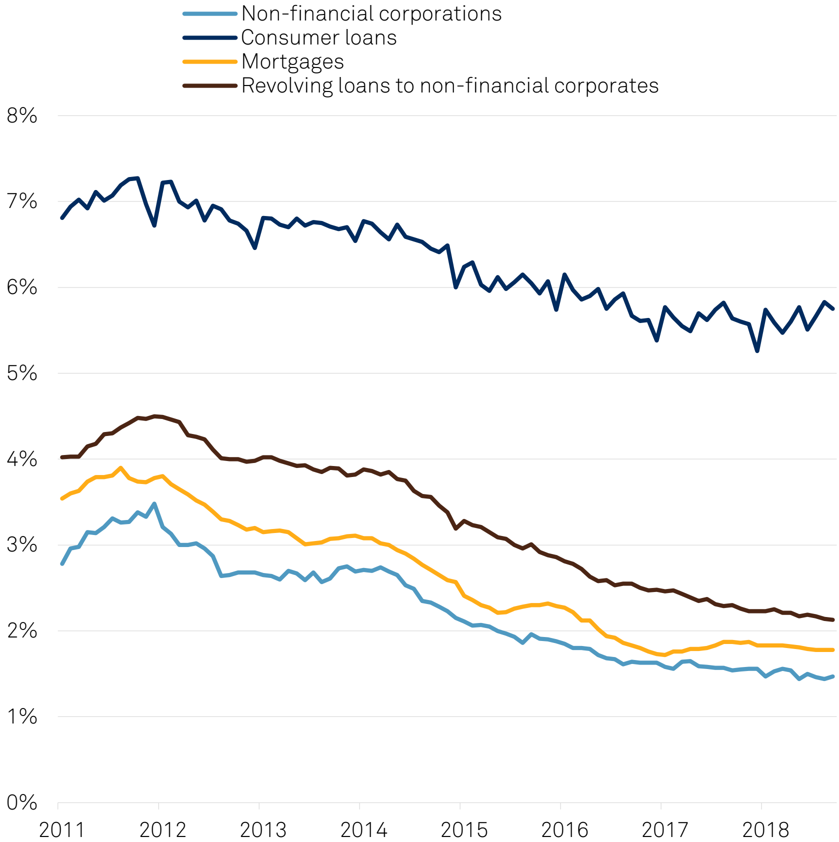


Data covers top 50 European banks (where available), plus selected U.S., Canadian and Australian majors for comparison purposes. Data as of Dec. 31, 2015, Jan. 21, 2018, Oct. 12, 2018.

Source: S&P Capital IQ.

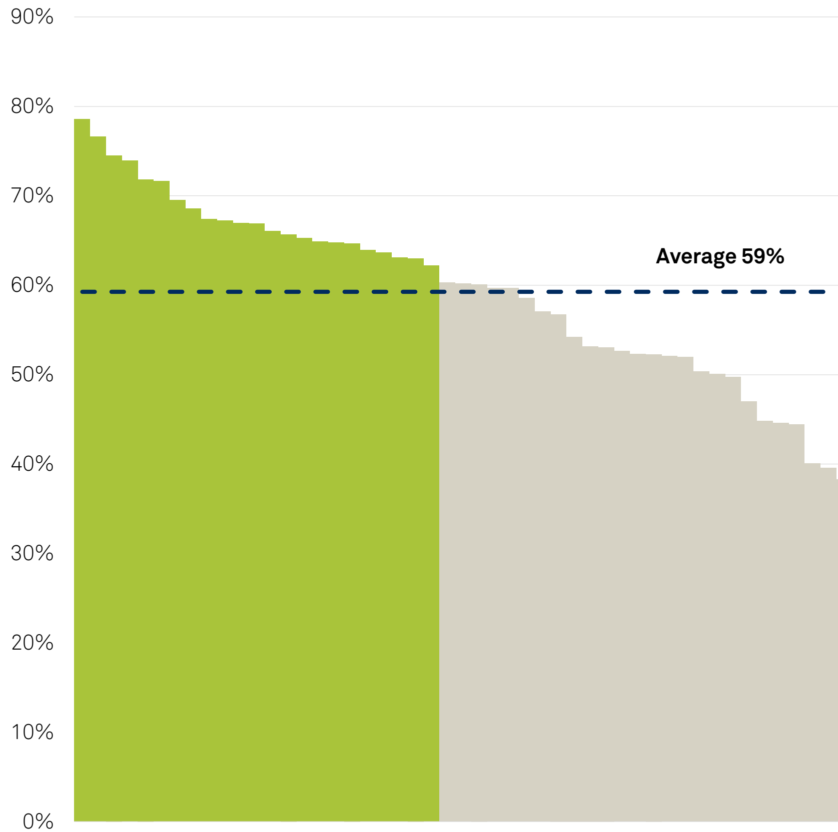
Banks Need To Focus On Efficiency

Interest Rate On New Lending, Euro Area



European Central Bank Statistical Data Warehouse.

European Top 50 Banks - Forecast Of 2019 Cost-To-Income



Data as of Oct. 31, 2018. The average and chart excludes data for Dexia S.A. Source: S&P Global Ratings.

Scope For Consolidation But Cross-Border Mergers Is Premature

Domestic Consolidation Has Driven European Bank M&A

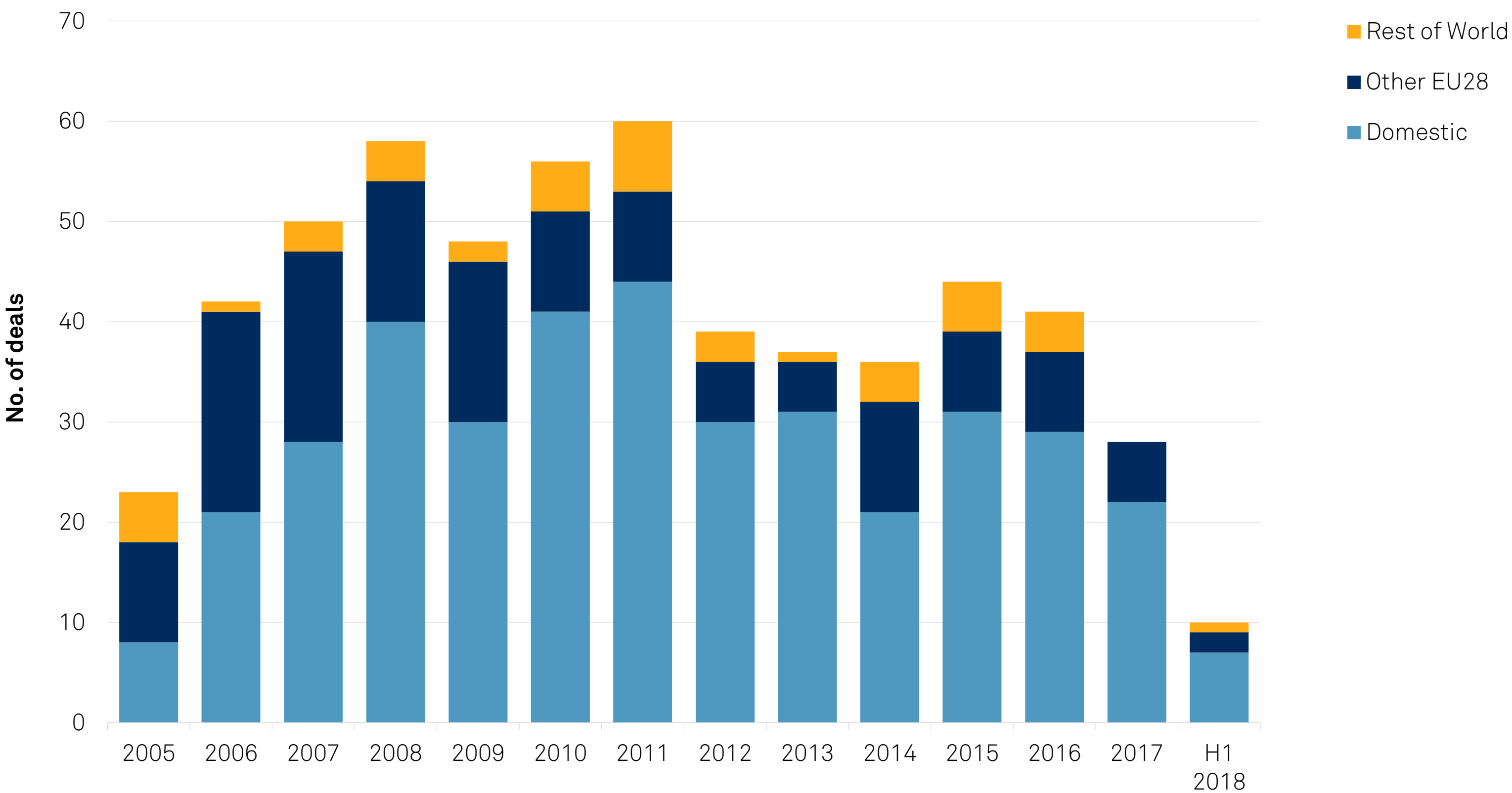


Chart shows the number of EU28 banks acquired by other banks, split by the buyer's location.

Source: S&P Global Market Intelligence.

Asia-Pacific Banks

Key Expectations

- The majority of rating outlooks are currently stable, and our base case is that this trend is likely to continue into 2019.
- Asset quality should remain relatively stable. Nonperforming loans should remain relatively low in some jurisdictions (including Taiwan, Australia, New Zealand, Singapore, Hong Kong, and Japan) but will remain much higher in some others, notably India.
- The earnings and capital outlook for banks in many jurisdictions remains broadly supportive of ratings at current levels.
- We see little rating upside but some notable downside risks that could affect ratings. We expect that most banks can weather a moderate and gradual downside scenario outside our base case at current rating levels. A significant and abrupt credit cycle downturn, however, will likely result in negative ratings momentum for some Asia-Pacific banks.

Key Assumptions

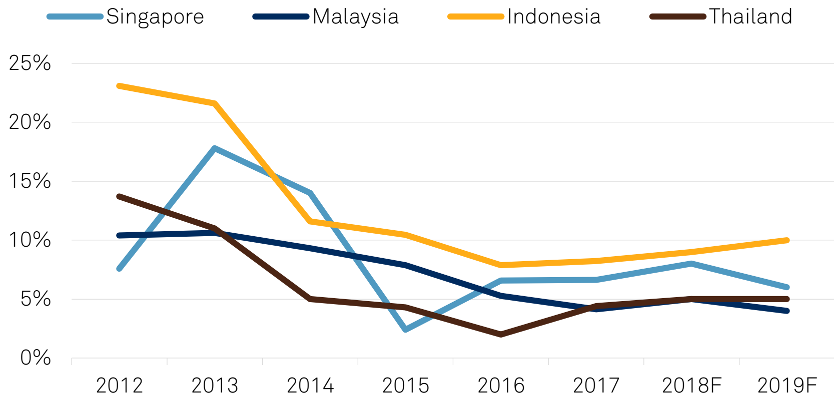
- Macroeconomic conditions are softening and we are cautious about a potential deterioration in credit conditions precipitated by higher U.S. interest rates and more volatile domestic currencies.
- Systemically important private-sector banks should continue to benefit from government support in most jurisdictions.

Key risks

- There are currently high debt levels and asset prices noting that interest rates have been low for a long time. These factors set the stage for a potential deterioration in credit quality, especially if there is a sharp correction in asset prices and pullback in market liquidity.
- The existing environment of depreciating domestic currencies and skittish bond markets, as well as expectations for higher interest rates and more difficult financing conditions in 2019, pose additional risks and further challenges for banks.

ASEAN: Well-Positioned Against Headwinds

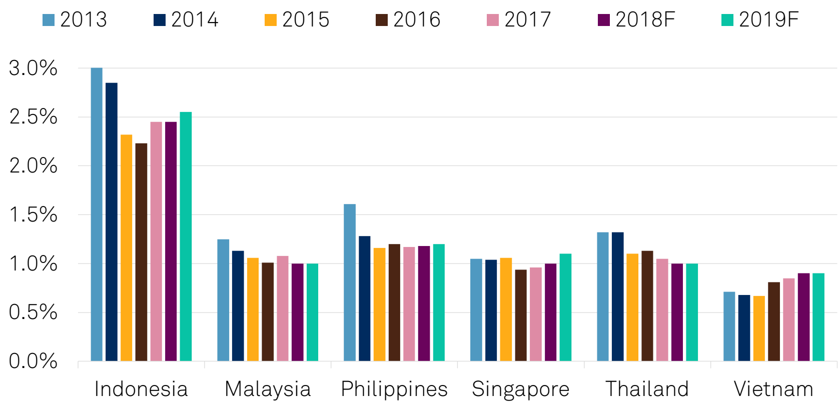
Long-Term Trend Of Declining Loans Growth



F--Forecast. Source: S&P Global Ratings.

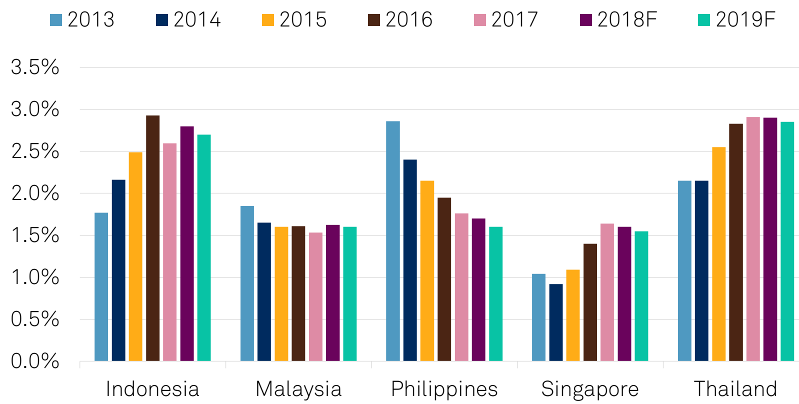
- ASEAN banks will continue to experience modest growth due to headwinds from trade war and emerging currency sell-off.
- Profitability remains good despite margin pressure, thanks to cost control measures and lower provisioning costs.
- Asset quality measured by reported nonperforming loans has either stabilized or declined.
- ASEAN banks have good capital levels, having accumulated buffers during previous years, and are well-positioned to face external headwinds.

ROA Of ASEAN Banks – Reasonable Returns



F--Forecast. Source: S&P Global Ratings.

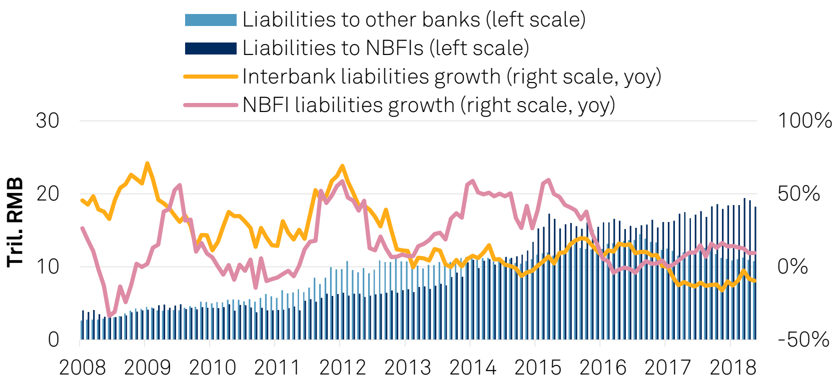
Asset Quality Trends – Ratios Look Healthy



F--Forecast. Source: S&P Global Ratings.

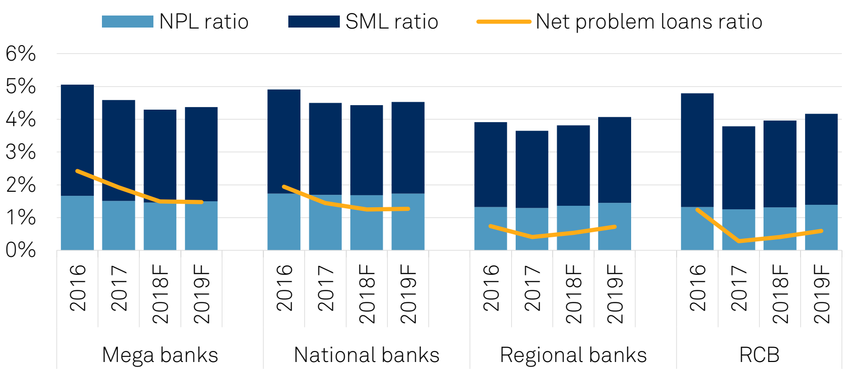
China: Deleveraging While Disseminating

Stagnating Growth In Interbank Liabilities



NBFI—Nonbanking financial institution. Source: S&P Global Ratings.

Trend In Loan Quality Of China's 41 Listed Banks By Peer Group

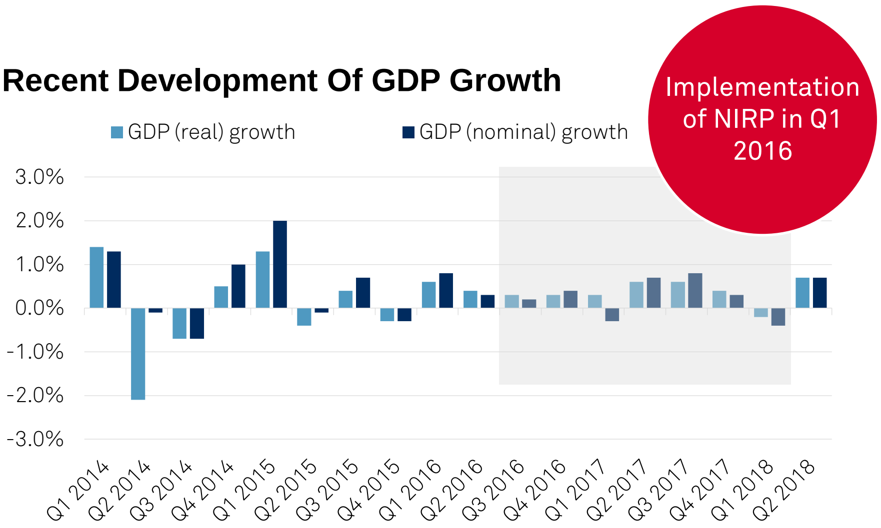


F--Forecast. Net problem loans refer to the sum of nonperforming loans (NPL) and special-mention loans (SML), net of loan loss reserves. Sources: Banks' annual and interim reports, S&P Global Ratings.

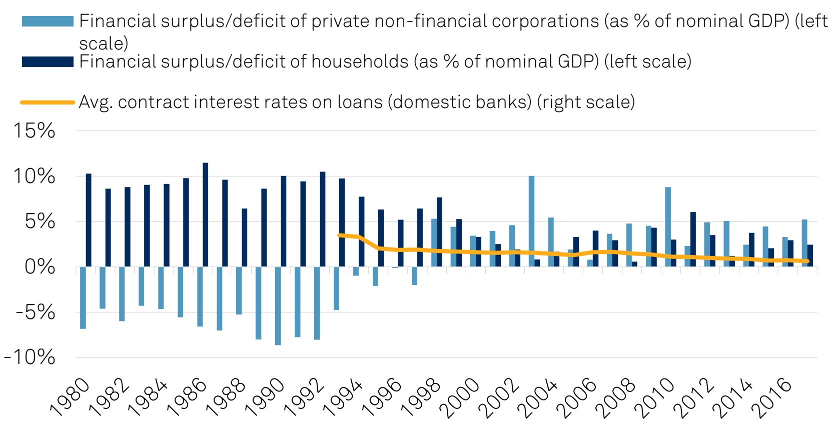
- The risk of a disorderly deleveraging seems to be stabilizing. This is evidenced by slower credit growth, lower shadow banking and interbank lending, letting yields rise in a controlled manner, and allowing for more defaults (although we expect them to remain very low).
- However, the ongoing trade dispute with the U.S. continues to heighten and has the potential to spill over into finance, investment, and business confidence. If the dispute drags on, it would pose a significant risk to corporate profitability and cash flow and add pressure on asset quality and profitability of banks.
- We expect asset quality to slightly worsen over the next two years due to tighter lending conditions under financial and corporate sector deleveraging policies, corporates refinancing at higher interest rates, and more stringent rules on nonperforming loan recognition.
- With strong funding bases and ample regulatory capital buffers, megabanks are significantly better placed to disseminate credits than the smaller banks.
- The housing market is likely to soften with both the prices and sales volume of new units to decline in 2019. We expect sales to decline by 8%-12%, and prices to drop by up to 5%.

Japan: Weakening Profitability Despite GDP Rebound

Recent Development Of GDP Growth



Private Sectors Have Been In A Surplus Position



NIRP's Side Effects Emerge Strongly

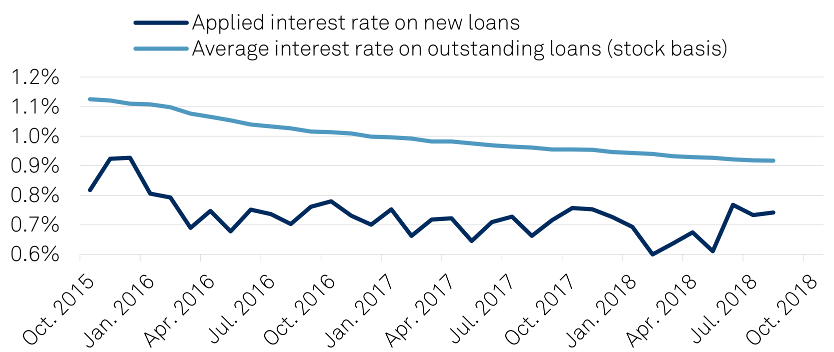
— Japan's negative interest rate policy (NIRP) seems to have bolstered current domestic economic growth.

— However, NIRP did not push up lending demand due to a funding surplus in private sectors.

— As loan growth remains very limited, banking sector margins are narrowing.

— Our credit analysis of Japanese banks is centered on whether their risk appetite will remain subdued, even as their profitability declines.

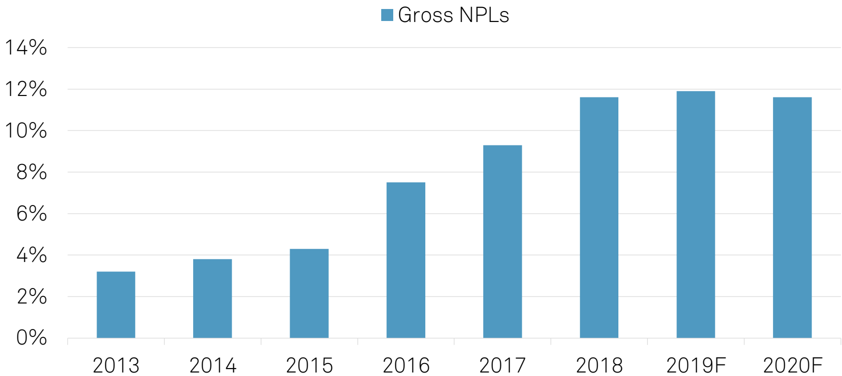
Domestic Banks/Contract Interest Rate: New Loans And Outstanding Loans



Sources: Government data, S&P Global Ratings analysis.

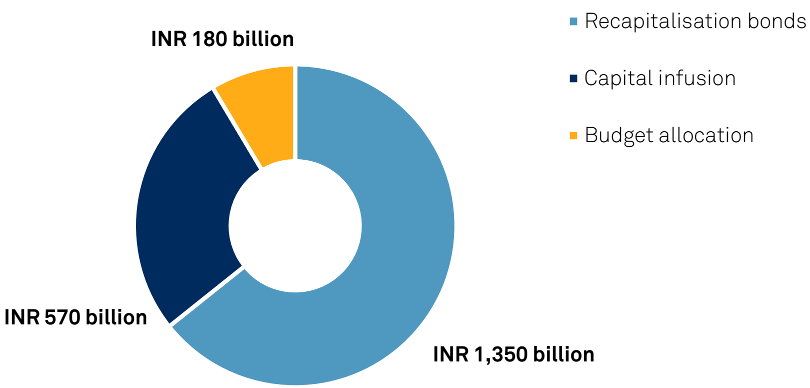
India: 4Rs Strategy Could Strengthen Banks

Better Recognition Of NPLs



Fiscal year data. F--Forecast. NPLs--Nonperforming loans. Source: Reserve Bank of India.

India's INR 2.1 Trillion Recap Program Will Primarily Rely On Government



INR--Indian Rupee. Source: Government of India, S&P Global Ratings' estimates.

Resolution of NPLs

— We assess that up to 15% of loans are problematic and a large proportion has been recognized. Large NPLs resolution is expected in 2019 under the new bankruptcy law. Rebounding corporate performance will support future asset quality.

— The government put in place a large recapitalization plan of $32 billion to address weak capital in state banks. We expect continued losses for many public-sector banks in fiscal 2019.

— We expect the banking sector's performance to gradually recover from fiscal 2020,but could face a delay if currency depreciation or finance company liquidity reduction impact banks.

The Missing R: Reform Banks

— The fraud case at Punjab National Bank highlights weak internal controls and vulnerabilities in risk management at Indian banks.

— If successfully implemented, the reform has the potential to strengthen the sector over time.

— However, very few steps have been taken so far on the reform front and follow-through on announced reforms has been weak. Bank consolidation is gaining momentum, but may not yield desired results without reforms.

Australia: Pressures Seem To Be Easing On Government Support And Imbalances

— Outlooks on major banks and Macquarie Bank remain negative reflecting potential for weakening in government support but recent APRA (Australian Prudential Regulation Authority) proposal indicates that this pressure is receding.

— Economic imbalances remain elevated. However, low credit growth and small falls in house prices in the past year, along with our expectation that credit losses will remain very low, suggest an orderly unwinding of risks.

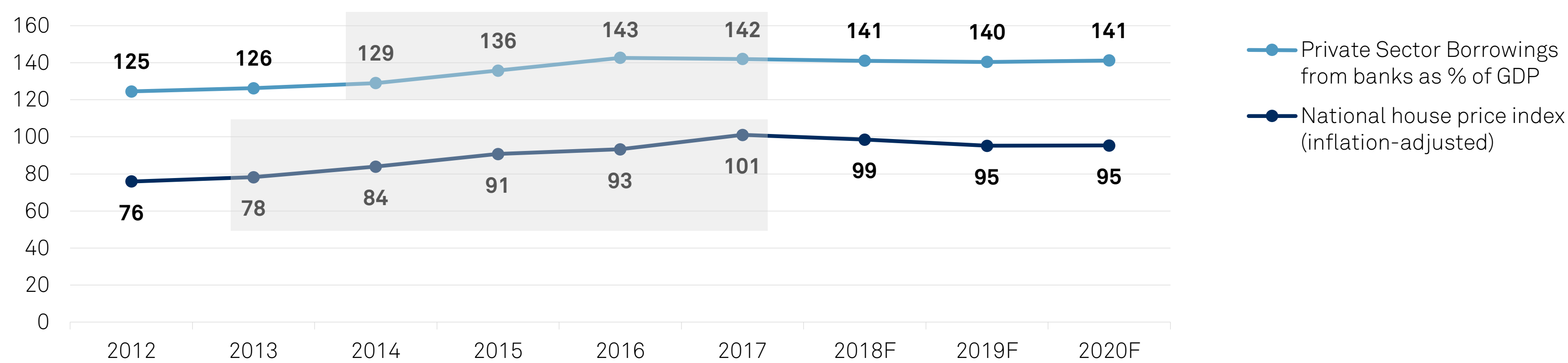
— Earnings growth is likely to be subdued due to pressures on interest margins and lending growth, and possible costs emerging from the Royal Commission into misconduct in the financial services industry.

Scenario Analysis: Australian Major Bank Ratings

			A major Australian bank	
Australia scenarios	**Government supportiveness**	**Sovereign local currency ratings**	**Stand Alone Credit Profile (SACP)**	**Issuer Credit Rating (ICR)**
Base-case	Highly supportive	AAA	a-	AA-
Scenario 1	Supportive	AAA	a-	A+
Scenario 2	Highly supportive	AAA	a	AA-
Scenario 3	Supportive	AAA	a	A+

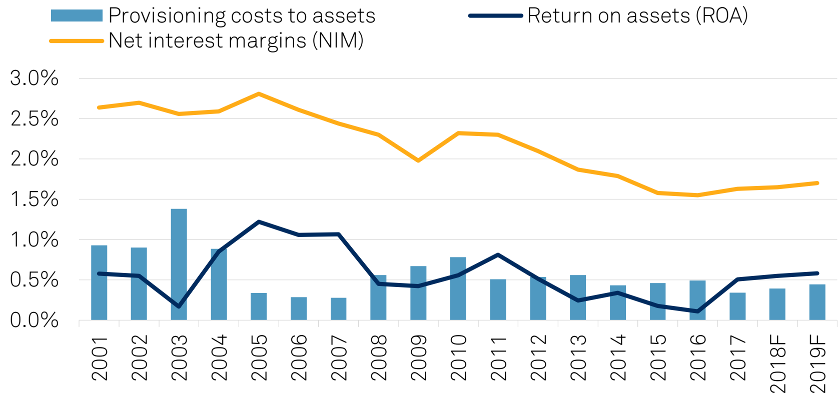
SACP / ICR	No change	1 notch better	1 notch worse

Imbalances in Australia Showing Signs of Easing



Korea: Navigating Uncertain Conditions

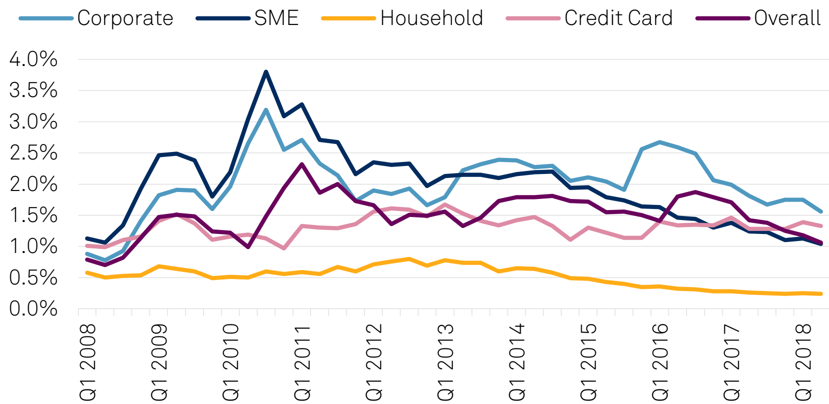
Profitability And Provisioning Costs



Source: Financial Supervisory Service, S&P Global Ratings. F--S&P Global Ratings' forecast.

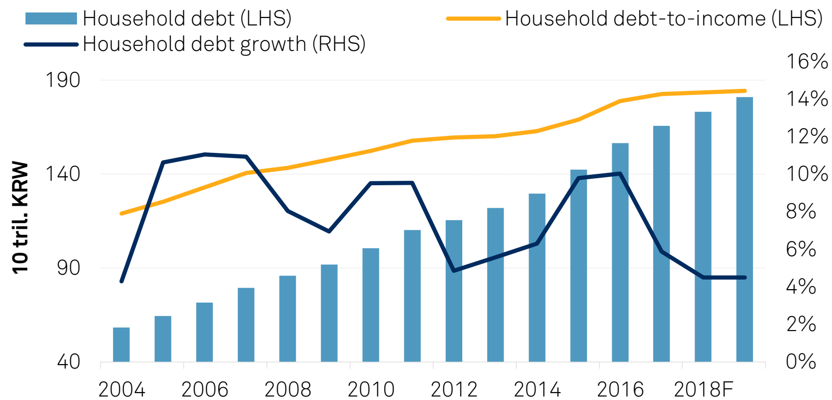
- Broadly stable financial performance, supported by improving net interest margins and moderate growth appetite, despite uncertain economic conditions given U.S-China trade conflict, weaker domestic housing demand, and U.S. interest rate rise.
- Potential credit risks mitigated by overall improvement in asset quality in recent years.
- High household debt (at about 95% of GDP) remains a risk, particularly if interest rates surge or household income suddenly drops.
- A resolution regime that includes the bail-in of senior creditors may result in some downgrades of systemically important banks.

NPL Ratios By Loan Type



Source: FSS, S&P Global Ratings.

Household Debt And Debt-To-Income

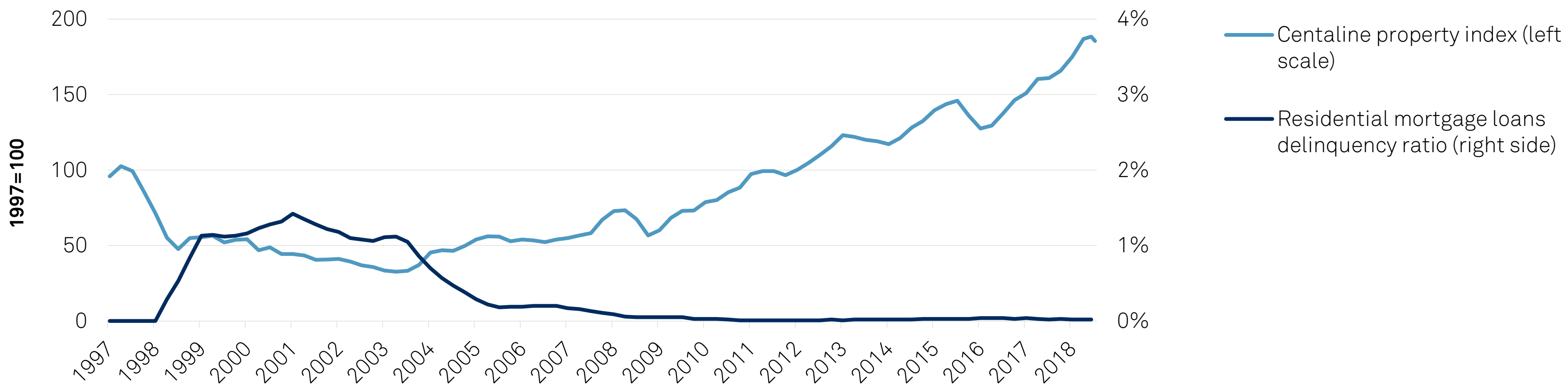


Source: Bank of Korea, S&P Global Ratings.

Hong Kong: Moderating Property Prices And Credit Growth To Temper Risk

- Reasonably prudent underwriting practices, backed by tight regulatory monitoring and some improvement in overall asset quality, provide a cushion for economic uncertainties about U.S.- China trade tensions and rising interest rates.
- Contained decline in property prices (5%-10%) expected in 2019.
- Broadly stable financial performance outlook backed by interest margin expansion and moderate growth.

Delinquencies Remained Low After 1997 Housing Crash



Source: Bloomberg, Centa-City Index, Hong Kong Monetary Authority, S&P Global Ratings.

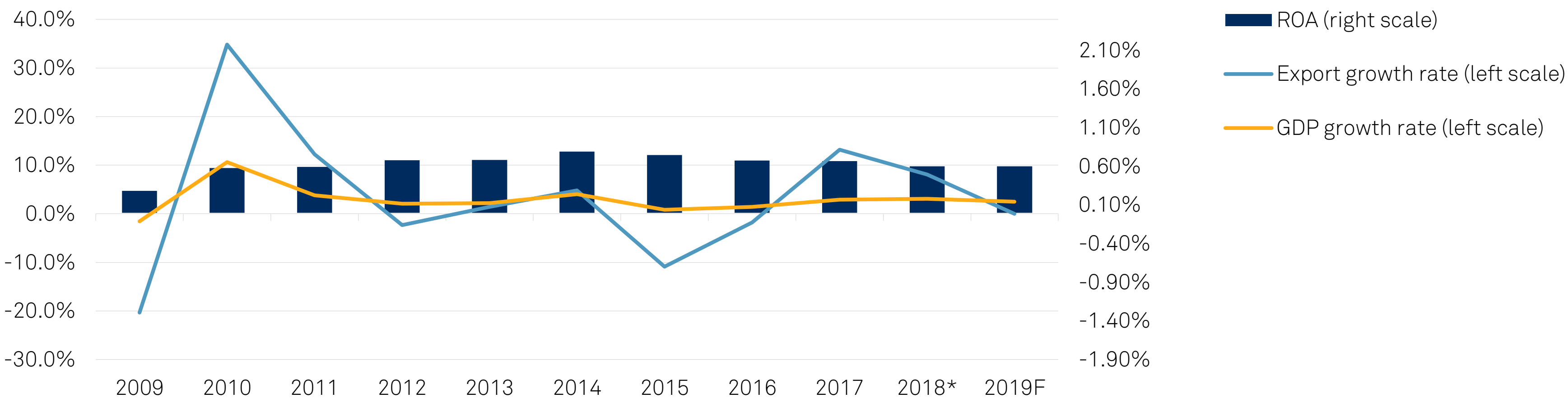
Taiwan: Uncertainty Of Trade Tension Pressures Moderate Profitability

— Global trade tension could negatively affect Taiwan's GDP, ultimately weighing on the banks' credit profile given the export oriented economy.

— Taiwan-based banks' profitability is expected to remain low in 2019.

— Solid capitalization under Basel III requirements underpin banks' credit profiles and stable outlooks.

Slower Expected Export Growth Rate Lead To Moderate Economic Growth In Taiwan



Export data are for the first nine months of 2018. GDP and ROA are 2018 estimated figures.
Source: National Statistics R.O.C. ©Taiwan Ratings Corp. 2018.

Latin American Banks

Key Expectations

— We expect Latin American banks to remain resilient amid an expected less favorable economic environment and investors' increasing risk aversion to emerging markets and currency weakening. Banks in Latin America's largest banking sectors have had conservative growth strategies and low dependence on external funding, while maintaining sound provisioning coverage and healthy interest margins.

— Credit demand has remained subdued in the largest economies due to weak investor confidence and economic performance. However, better economic prospects in 2019 will support higher credit demand. We expect asset quality to remain healthy and profitability strong.

Key Assumptions

— The U.S., Canada, and Mexico agreed on a new trade arrangement to replace the NAFTA--which the respective congresses need to ratify--that will largely preserve the cross-border trade and financial links that underpin the North American economies.

— We expect interest rates to increase gradually and banks to transfer the higher funding costs to ultimate borrowers.

— Credit losses have picked in 2018 and will stabilize or improve from 2019. Loan growth will follow a similar pace than economic growth, while credit penetration will grow modestly.

— Relatively low exposure to foreign exchange risk will allow Latin American banks, in general, to remain resilient amid potential volatility of some currencies.

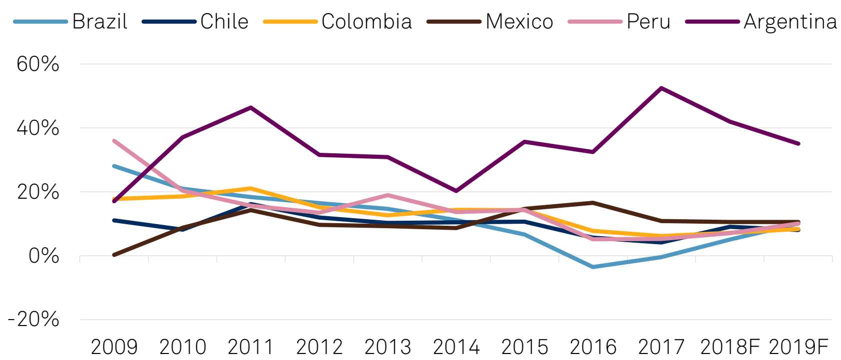
Key risks

— Political uncertainties prevail. Now that new presidents were elected in Colombia, Mexico and Brazil, we will monitor if there are significant changes in economic policies.

— Higher inflation due to weakening exchange rates and increasing interest rates could pressure household debt payment capacity, especially in Argentina where we saw the steepest currency devaluation and highest inflation.

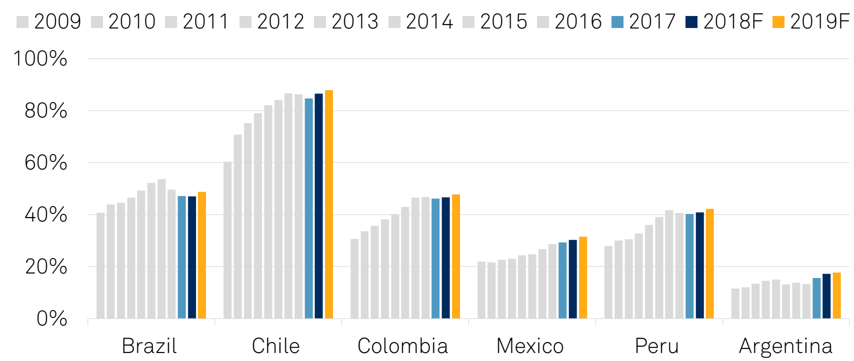
Latin American Banks

Nominal Loan Growth



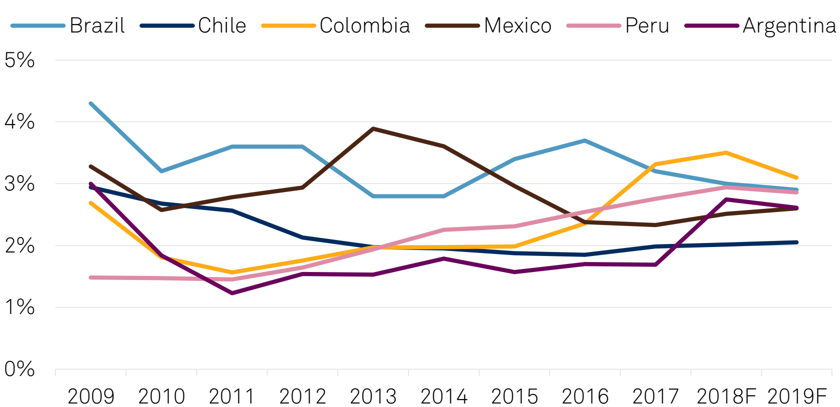
Source: S&P Global Ratings.

Penetration (Total Credit / GDP)



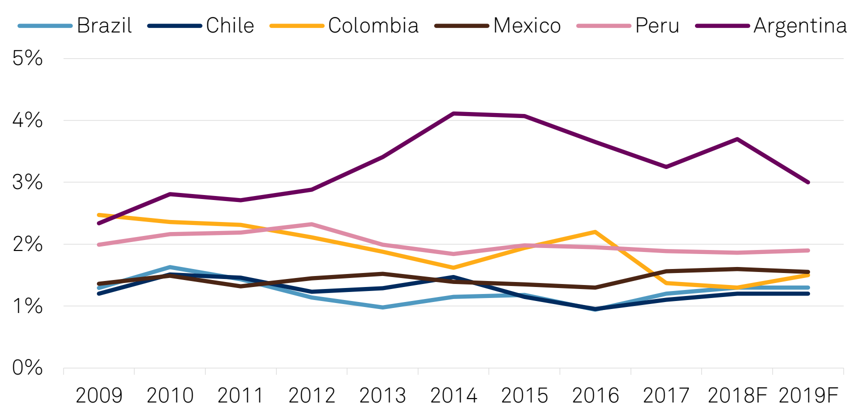
Source: S&P Global Ratings.

Nonperforming Assets As A % Of Systemwide Loans



Source: S&P Global Ratings.

Systemwide Return On Average Assets



Source: S&P Global Ratings.

Latin American Banks Outlook

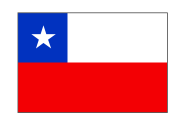
Brazil

- After Jair Bolsonaro's election, Brazil is closing a chapter on the massive corruption case—Lava-Jato—and pushing ahead with promised widespread reforms. However, the incoming administration will have major challenges in translating campaign rhetoric into actual reforms. We expect GDP growth of 1.4% in 2018 to strengthen to 2.4% in 2019.
- We believe domestic banks are well positioned to provide funding to companies that will likely need to redeem investing, which should boost lending to about 10% in 2019 after years of subdued growth.
- Banks' asset quality metrics will likely continue improving supporting healthy operating performance. We also expect growth in lending among private banks to continue outpacing that of their public peers.

Mexico

- Uncertainty about long-term economic policies that the new Mexican administration of Lopez Obrador (AMLO) will implement remains significant. Recent developments surrounding the construction of the new airport in Mexico City have raised investor concerns about the potential direction of policies.
- The Senate leader of AMLO's party recently presented an initiative in the Mexican congress to eliminate certain banking fees and commissions, most of them related to credit cards. If the proposal becomes effective, banks' operating revenues would drop by about 7%. In general, this should not affect our ratings on banks.
- We expect loans to grow at a moderate pace in 2019 as economic growth remains relatively stumpy--we project real GDP growth at 2.2% next year and 2.4% in 2020--and external conditions deteriorate. Loan growth will follow a similar pace to economic growth, with credit penetration growing modestly.
- Asset quality indicators will likely remain at healthy levels, with nonperforming assets projected at about 2.5%, given low unemployment rates, rising real wages, and a somewhat smaller informal economy (although it remains large).

Chile



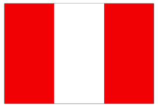
- Economic prospects in Chile have improved because of renewed business confidence. This will support banks' operating performance and asset quality metrics.
- In October 2018, the Chilean Senate approved a new banking law that aims to align the country with Basel III principles. Banks are generally well prepared to withstand the new capital requirements, although some will likely consider issuing AT1 (Additional Tier 1) instruments once the regulation is in place.

Latin American Banks Outlook

Argentina

- Investor sentiment toward emerging markets has turned sour, causing funds to shift away from several emerging markets, including Argentina, which suffered a steep depreciation of its currency.
- The combination of Argentina's additional fiscal austerity and monetary tightening may help stabilize the exchange rate and contain inflation, but will cause GDP to contract by 2.5% in 2018 and 0.8% in 2019.
- The Central Bank is fighting inflation by reducing pesos in circulation, maintaining the monetary base constant, increasing the reserves requirements, and increasing interest rates.
- Higher interest rates, inflation, and weaker economic activity will likely hurt asset quality metrics of banks.
- Banks' conservative strategies will help them cope with the difficult economic conditions and volatile exchange rate, focusing on higher-income segments and corporates and only lending in dollars to dollar generators.

Peru



- Investor and business confidence showed signs of recovery after a long period of political turbulence.
- We expect credit growth to reach about 10% in 2018 and 2019 after two years of low credit growth, and asset quality to stabilize.

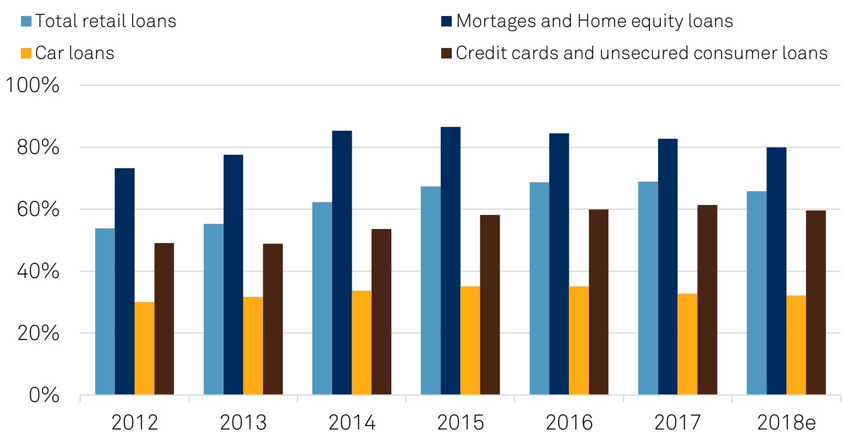
Colombia

- Colombia's real GDP growth will stand at 2.9% in 2019--after growing by an estimated 2.6% in 2018--considering that the Duque administration will likely pursue similar market-oriented economic policies.
- However, a potential new tax reform could disincentive consumer demand, increase inflation, and slow the economic expansion.
- After the dip in asset quality during 2016-2017, we expect nonperforming assets to gradually recover to around 3% in 2019-2020.

Russian Banks: Under Pressure Of Sanctions

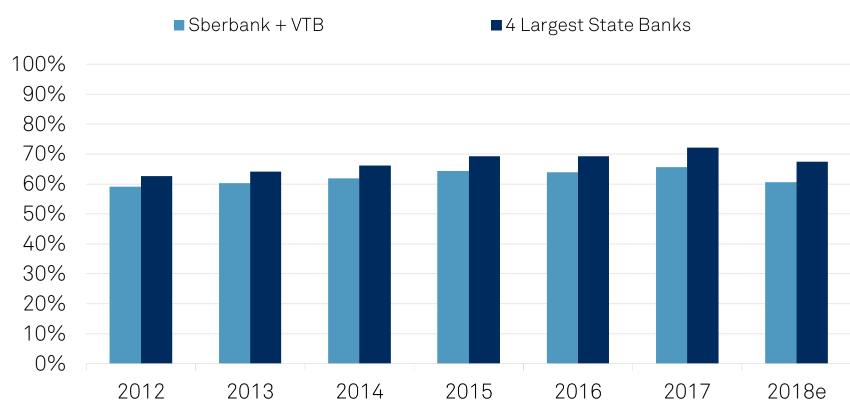
- Sanctions are significantly constricting capital flows and the ability of banks to borrow abroad.
- Domestic deposits will remain the key source of funding for the baking sector. Their stability will be dependent on the recovery of macroeconomic fundamentals and vulnerable to additional sanctions.
- The dominant market position of state banks is leading to increasing competitive pressure for smaller private banks.
- A structural lack of long-term funding, alongside economic sanctions, and volatile market confidence will continue to weigh on the funding profiles of Russian banks.
- Domestic capital markets remain undeveloped and limited access to external markets continues to restrict Russian banks' and their borrowers' access to long-term funding. Although currently manageable, this might restrict banks' ability to finance mortgages, infrastructure, and other long-term loans.
- Capitalization of the sector remains weaker than most peers'.

Market Share Of Sberbank And VTB In Retail Lending



e--Estimate. Source: CBR, Sberbank, VTB, S&P Global Ratings.

Market Share Of State Banks In Retail Deposits

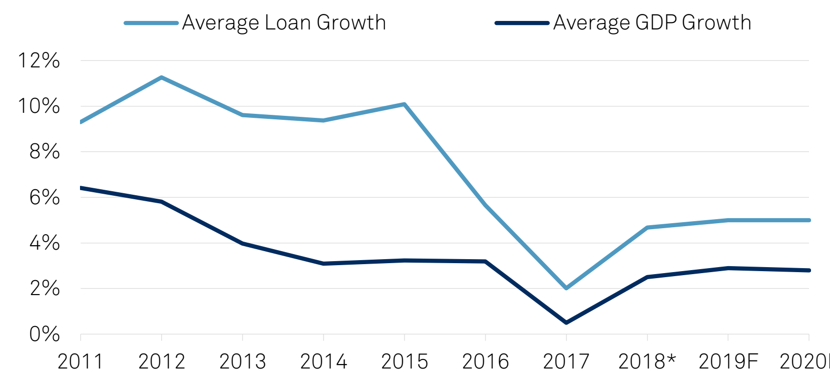


e--Estimate. Source: CBR, S&P Global Ratings.

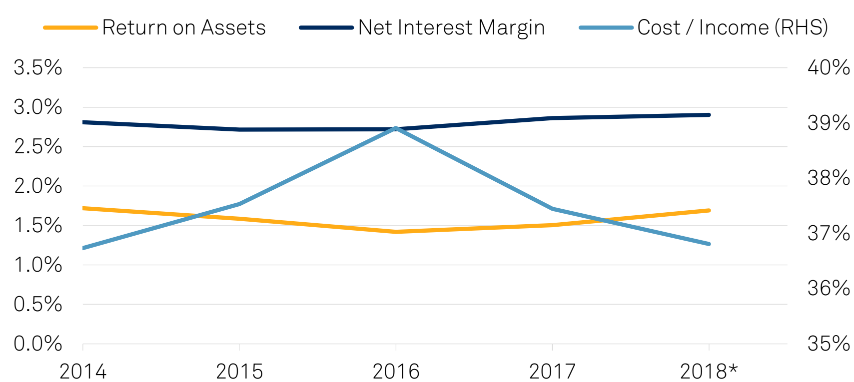
GCC Banks: Geopolitical Risk Or Oil Prices Could Destabilize The Outlook

- GCC (Gulf Cooperation Council) banks' financial profiles should remain stable in 2019, absent any unexpected geopolitical shock. However, the recent drop in oil prices does not bode well for these banking sectors.
- Bank lending growth should stabilize at around 5% in 2019, as stronger public investments raise economic growth in the region overall.
- We expect profitability to stabilize--with a return on assets at about 1.6% and a net interest margin at 3% in 2018--benefitting from the higher interest rates and significant non-interest-bearing deposits.
- International operations could create risks for some GCC banks. A few banks with exposure to Turkey will see some impact on their asset quality.
- Three-quarters of the 24 GCC rated banks carry a stable outlook. Negative outlooks are concentrated in Qatar and on a few banks in other GCC countries due to higher risk in their international operations. The average GCC bank rating is 'BBB+'.

Growth Of GCC Banks Loan Portfolios Versus GDP Growth



Rated GCC Banks Profitability Indicators

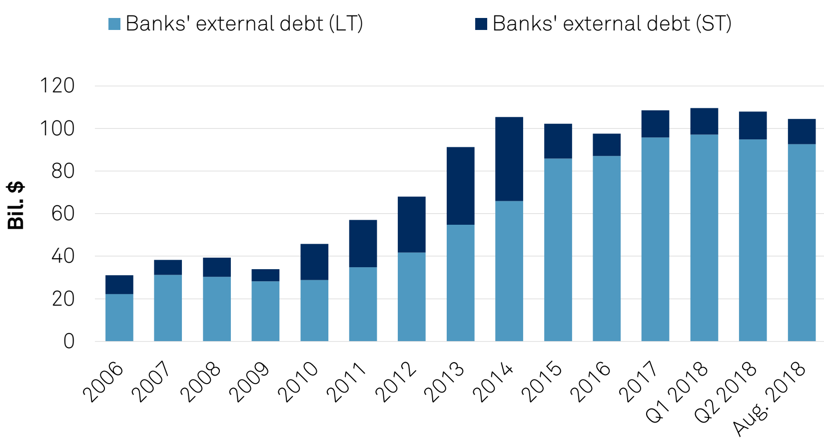


*Data as of end June, 2018. Annualized data where applicable. Source: S&P Global Ratings.

Turkish Banks: External Debt Is Key Risk

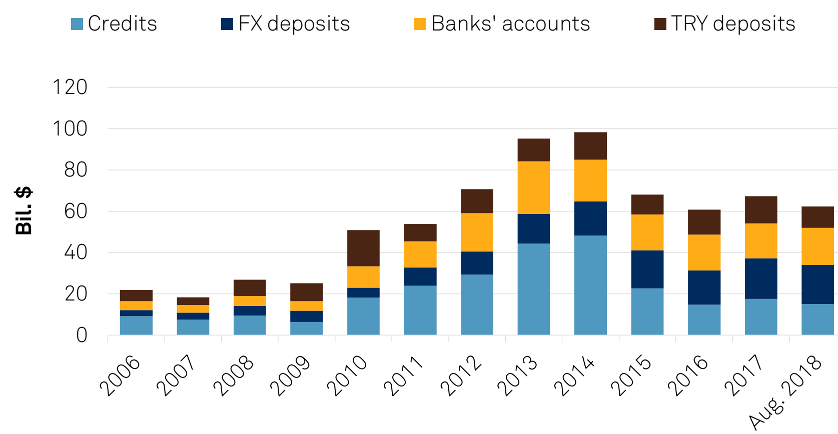
- External debt is high and exposes banks to shifts in external financing conditions, despite the sharp turnaround of Turkey's current account position. The sharp depreciation of the Turkish lira (despite its recent rally) and the uncertainty related to policy direction weighed on investor sentiment and led some corporates and nonbank financial institutions to default.
- Refinancing risk peaked during the summer, when markets were not accessible over a short period of time. Since then, market access has somewhat improved, with several banks refinancing their debt with high rollover rates, albeit at higher cost.
- Banks have large foreign currency denominated assets (about $95 billion at Sept. 30, 2018), but if rollover rates drop below a certain level or if banks lose significant amounts of other short-term debt, the risks will be displaced to the Central Bank balance sheet.
- Other main risks include the deterioration in asset quality and pressure on capitalization. We estimate problematic assets to be close to 20% of total loans, driven by the economic slowdown (we forecast a 0.5% decline in real GDP in 2019), increased interest rates, and lira depreciation. Banks' capitalization is also declining under the joint effect of lira depreciation and marked-to-market losses on government bonds.

Turkish Banks' Commercial External Debt



LT--long-term. ST--short-term. Source: S&P Global Ratings.

Turkish Banks Other Short-Term Debt



Source: S&P Global Ratings.

South African Banks: Stability In A Weak Operating Environment

— Anemic economic growth in 2018 and sizable contingent liabilities continue to weigh on South Africa's fiscal prospects and debt burden. Nevertheless, the new government is pursuing economic reforms that should help boost the economy (GDP growth is expected to reach 1.8% in 2019), despite structural impediments, chronic skills shortages, and high unemployment.

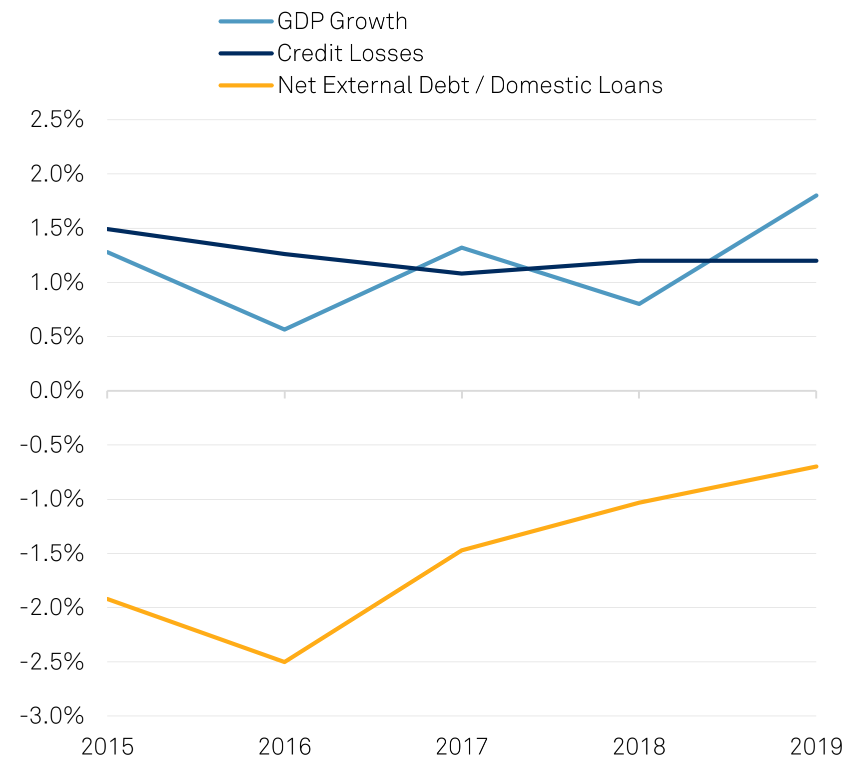
— If the rule of law, property rights, or enforcement of contracts were to weaken significantly, this would undermine the investment and economic outlook, and ultimately the banking sector.

— Increasing inflation is expected to put additional pressure on households creditworthiness and banks' asset quality. Overall, we expect credit losses to reach 1.2% in 2019.

— Lending in foreign currency remains limited (less than 10% of total lending) and dependence on external funding is marginal. However, dependence on local wholesale funding is a source of risk for South African banks that is partially mitigated by exchange control.

— Banks benefit from good regulation and supervision, as well as an oligopolistic structure of the system that protects their profitability. At the same time, some small banks have recently been hit by governance issues.

Credit Losses Remain Under Control



Source: S&P Global Ratings.

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